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John F. Connolly

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LIMITS ON RESIDENTIAL MORTGAGE LENDER PROTECTION UNDER SECTION 1322(b)(2) OF THE BANKRUPTCY CODE

INTRODUCTION

One of the primary purposes of the Bankruptcy Reform Act of 1978 (Bankruptcy Code) is to allow debtors "a fresh start, free from creditor harassment and free from the worries and pressures of too much debt."¹ Chapter 13 of the Bankruptcy Code grants this "fresh start" by offering individuals with regular income relief from creditors while allowing the individuals to protect their assets.² Chapter 13, consequently, offers debtors an alternative to liquidation of their assets under Chapter 7.³ Instead of liquidation, Chapter 13 provides for debtors to repay their creditors through an installment plan.⁴ Under the installment plan, an individual makes "periodic payments to a trustee under bankruptcy court protection, with the trustee fairly distributing the funds deposited to creditors until all debts have been paid."⁵ Creditors may receive partial or full payment under the Chapter 13 plan.⁶

Section 1322⁷ of the Bankruptcy Code establishes the

1. H.R. REP. NO. 595, 95th Cong., 1st Sess. 125 (1977), *reprinted in* 1978 U.S.C.C.A.N. 5963, 6086.

2. H.R. REP. NO. 595, 95th Cong., 1st Sess. 118 (1977), *reprinted in* 1978 U.S.C.C.A.N. 5963, 6079.

3. *Id.*

4. 11 U.S.C. § 1322 (1988). Subsection (c) of this statute states: "The plan may not provide for payments over a period that is longer than three years, unless the court, for cause, approves a longer period, but the court may not approve a period that is longer than five years." *Id.*

5. S. REP. NO. 989, 95th Cong., 2d Sess. 12 (1978), *reprinted in* 1978 U.S.C.C.A.N. 5787, 5798.

6. H.R. REP. NO. 598, 95th Cong., 1st Sess. 118 (1977), *reprinted in* 1978 U.S.C.C.A.N. 5963, 6079.

7. 11 U.S.C. § 1322 (1988). The statute reads in relevant part:

(a) The plan shall—

....

(2) provide for the full payment, in deferred cash payments, of all claims entitled to priority

....

(b) Subject to subsections (a) and (c) of this section, the plan may—

procedure for determining whether a creditor will receive partial or full payment from a Chapter 13 debtor.⁸ Section 1322(b)(2),⁹ however, prevents a debtor from reducing her payments to a creditor who holds "a claim secured only by a security interest in real property that is the debtor's principal residence."¹⁰ The intent of this exception is to protect the mortgage industry and the home sale markets.¹¹ This protection is required because the "American Dream" of an individual owning her own home is dependent on low down payments and insurance programs to recover banking foreclosure losses.¹² Without protection to ensure that lender losses will be minimized, requirements for extending home loans would have to be raised to lower losses; the effect of higher standards would place the initial cost of mortgages beyond the reach of many buyers.¹³

The extent of the protection of § 1322(b)(2), however, is a subject of contentious debate. The language of § 1322(b)(2) is ambiguous and the congressional intent is unclear.¹⁴ On one side, lenders contend that § 1322(b)(2) was specifically written to afford them protection¹⁵ and that without this protection

. . . .
(2) modify the rights of holders of secured claims . . . or of holders of unsecured claims.

Id.

8. *Id.*

9. 11 U.S.C. § 1322(b)(2) (1988). The statute reads:

[The Chapter 13 plan may] modify the rights of holders of secured claims, other than a claim secured only by a security interest in real property that is the debtor's principal residence, or of holders of unsecured claims, or leave unaffected the rights of holders of any class of claims.

Id.

10. *Id.*

11. Michael S. Polk, *The Chapter 13 Cramdown: New Nightmare for the Lender*, 19 REAL EST. L.J. 279, 290 (1991).

12. *Id.* at 297-98.

13. *Id.*

14. *Wright v. C&S Family Credit, Inc. (In re Wright)*, 128 B.R. 838, 845 (Bankr. N.D. Ga. 1991).

15. See, e.g., *In re Hall*, 117 B.R. 425, 428 (Bankr. S.D. Ind. 1990) (section 1322(b)(2)'s purpose is to provide stability in the residential long-term mortgage industry); *In re Williams*, 109 B.R. 36, 42 (Bankr. E.D.N.Y. 1989) (section 1322(b)(2) intended to protect traditional mortgage lenders who provide long-term financing that enables individuals to purchase their home); *Capital Credit Plan v. Shaffer*, 116 B.R. 60 (W.D. Va. 1988) (section 1322(b)(2) applies only to purchase money mortgages because intent of statute was to protect the home mortgage industry); *In re Shaffer*, 84 B.R. 63, 66-67 (Bankr. W.D. Va. 1988) (section 1322(b)(2) protection extends only

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underwriting standards would be tougher, interest rates would be higher, and many more home buyers, especially first-time buyers, would be denied mortgages.¹⁶ On the other side, debtors contend that there is no statutory prohibition to their "cramdown" proposals.¹⁷ Debtors allege that cramdown, which refers to the process by which a debtor is allowed to restructure a mortgage by reducing the "secured" value of the mortgage to the current fair market value of a home, is merely a result of bad lending decisions by banks, and that the banks should bear the consequences of such decisions.¹⁸

This Note examines the various techniques that debtors utilize to avoid the protection of holders of claims secured by the debtors' principal residence. The Note summarizes the various arguments supporting and opposing cramdown given the ambiguous language of § 1322(b)(2). Finally, this Note will examine recent decisions and their import for bankruptcy practice in Georgia.

to long-term home mortgages, which is the subject of § 1322(b)(2)'s plain intent), *aff'd sub nom.* Capital Credit Plan v. Shaffer, 116 B.R. 60 (W.D. Va. 1988); Cameron Brown Co. v. Bruce (*In re Bruce*), 40 B.R. 884, 887 (Bankr. W.D. Va. 1984) (section 1322(b)(2) protection extends only to purchase money mortgage lenders); United Cos. Fin. Corp. v. Brantley, 6 B.R. 178, 189 (Bankr. N.D. Fla. 1980) (intent of § 1322(b)(2) is to provide stability in the residential long-term home financing industry and market).

16. Todd Mason, *Lenders Cringe as Judges Chop Mortgage Value*, WALL ST. J., Sept. 26, 1990, at B1, B16.

17. See, e.g., Eastland Mortgage Co. v. Hart (*In re Hart*), 923 F.2d 1410 (10th Cir. 1991) (section 506(a) allows a debtor, without violating § 1322(b)(2), to reduce the value of a secured claim to the value of collateral); Wilson v. Commonwealth Mortgage Corp., 895 F.2d 123 (3d Cir. 1990); Houghland v. Lomas & Nettleton Co. (*In re Houghland*), 886 F.2d 1182 (9th Cir. 1989); Jim Walter Homes, Inc. v. Saylor (*In re Saylor*), 869 F.2d 1434 (11th Cir. 1989) (there is no statutory prohibition against the inclusion in a Chapter 13 plan of a mortgage debt which was previously discharged under Chapter 7); Downey Sav. & Loan Ass'n v. Metz (*In re Metz*), 820 F.2d 1495 (9th Cir. 1987); *In re Ward*, 129 B.R. 664 (Bankr. W.D. Okla. 1991); Secor Bank v. Dunlap, 129 B.R. 463 (E.D. La. 1991); Wright v. C&S Family Credit, Inc. (*In re Wright*), 128 B.R. 838 (Bankr. N.D. Ga. 1991); *In re Harris*, 94 B.R. 832 (D.N.J. 1989); *In re Lagasse*, 66 B.R. 41 (Bankr. D. Conn. 1986).

18. Mason, *supra* note 16, at B16; Vincent J. Canzoneri, *Cramdowns of Residential Mortgages in Declining Markets: The Perils and Potentials of Chapter 13*, 35 BOSTON B.J. 17, 18 (Aug. 1991); see also 11 U.S.C. § 506(a) (1988).

I. SECTION 1322(B)(2): PROTECTING WHOSE INTEREST?

A. Chapter 13 Cramdown Comes to Atlanta

Two recent cases have brought the issue of the extent of § 1322(b)(2)'s protection of the home mortgage industry to Atlanta.¹⁹ One case, *In re Smith*, has yet to be decided but sparked the initial publicity over the extent of § 1322(b)(2)'s protection.²⁰ *Smith* involves an attempt by a Suwanee family to remove an \$8,000 second mortgage on their home and convert the secured claim to an unsecured loan.²¹ This conversion of a secured loan to an unsecured loan is controversial because it appears to run afoul of the special protection afforded loans secured by debtors' homes in § 1322(b)(2).²² *Smith* argues, however, that § 506(a)²³ of the Bankruptcy Code allows him to bifurcate an undersecured claim into secured and unsecured portions, with the secured portion being equal to the value of the collateral.²⁴ Because the value of his home is \$78,000 and the first mortgage principal is \$78,547, *Smith* asserts that the second mortgage is undersecured and may be stripped away under § 506(a).²⁵

The other case, *Wright v. C&S Family Credit*,²⁶ involves an attempt by an Atlanta woman to bifurcate the undersecured first

19. See, e.g., *In re Smith*, U. S. Bankr. No. 91-60021 (N.D. Ga. filed Jan. 2, 1991); *Wright v. C&S Family Credit, Inc. (In re Wright)*, 128 B.R. 838 (Bankr. N.D. Ga. 1991).

20. See Tim O'Reiley, *Lien Stripping Comes to Atlanta*, FULTON COUNTY DAILY REP., April 26, 1991, at A1.

21. *Id.*

22. See 11 U.S.C. § 1322(b)(2) (1988) and *infra* notes 64-67 and accompanying text.

23. 11 U.S.C. § 506(a) (1988). The statute reads:

An allowed claim of a creditor secured by a lien on property in which the estate has an interest, or that is subject to setoff under section 553 of this title, is a secured claim to the extent of the value of such creditor's interest in the estate's interest in such property, or to the extent of the amount subject to setoff, as the case may be, and is an unsecured claim to the extent that the value of such creditor's interest or the amount so subject to setoff is less than the amount of such allowed claim. Such value shall be determined in light of the purpose of the valuation and of the proposed disposition or use of such property, and in conjunction with any hearing on such disposition or use or on a plan affecting such creditor's interest.

Id.

24. O'Reiley, *supra* note 20, at A4.

25. *Id.*

26. *Wright v. C&S Family Credit, Inc. (In re Wright)*, 128 B.R. 838 (Bankr. N.D. Ga. 1991).

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mortgage on her home into secured and unsecured claims pursuant to § 506(a).²⁷ The mortgagee, C&S Family Credit, objects to her Chapter 13 plan, arguing that it modifies the terms of a security interest in real property that is the debtor's principal residence and is thus in violation of § 1322(b)(2).²⁸

B. The Issue: The Meaning of § 1322(b)(2)

Section 1322(b)(2) provides that a Chapter 13 bankruptcy plan may "modify the rights of holders of secured claims, other than a claim secured only by a security interest in real property that is the debtor's principal residence, or of holders of unsecured claims."²⁹ Except for a claim secured by real property that is the debtor's principal residence, all claims secured by the personal or real property of the debtor may be modified in the debtor's Chapter 13 plan.³⁰ Likewise, a claim secured by both the debtor's principal residence and additional collateral may be modified under § 1322(b)(2).³¹ The case law on what constitutes such additional collateral, however, is not uniform. Liens on additional collateral which have been held to defeat lender protection include fixtures;³² mineral, oil, gas, and water

27. *Id.* at 840.

28. *Id.*

29. 11 U.S.C. § 1322(b)(2) (1988).

30. *Id.*; see also Peter H. Carroll, *Cramdown of Residential Mortgages in Chapter 13 Cases*, 20 COLO. LAW. 881, 881 (May 1991).

31. As examples of cases where specific items were found to constitute collateral in addition to the debtor's principal residence, see, e.g., *Eastland Mortgage Co. v. Hart* (*In re Hart*), 923 F.2d 1410 (10th Cir. 1991); *Wilson v. Commonwealth Mortgage Corp.*, 895 F.2d 123 (3d Cir. 1990); *Dent v. Associates Equity Serv. Co.* (*In re Dent*), 130 B.R. 623 (Bankr. S.D. Ga. 1991); *Secor Bank v. Dunlap*, 129 B.R. 463 (E.D. La. 1991); *Kessler v. Homestead Sav.* (*In re Kessler*), 99 B.R. 635 (Bankr. E.D. Pa. 1989); *Caster v. United States* (*In re Caster*), 77 B.R. 8 (Bankr. E.D. Pa. 1987); *In re Stiles*, 74 B.R. 708 (Bankr. N.D. Ala. 1987); *Johnson-Allen v. Lomas & Nettleton Co.* (*In re Johnson-Allen*), 67 B.R. 968 (Bankr. E.D. Pa. 1986); *In re Lapp*, 66 B.R. 67 (Bankr. D. Colo. 1986); *In re Reeves*, 65 B.R. 898 (N.D. Ill. 1986); *In re Hines*, 64 B.R. 684 (Bankr. D. Colo. 1986); *In re Ramirez*, 62 B.R. 668 (Bankr. S.D. Cal. 1986); *In re Foster*, 61 B.R. 492 (Bankr. N.D. Ind. 1986); *In re Leazier*, 55 B.R. 870 (Bankr. N.D. Ind. 1985); *In re Hilderbran*, 54 B.R. 585 (Bankr. D. Or. 1985); *United Cos. Fin. Corp. v. Brantley*, 6 B.R. 178 (Bankr. N.D. Fla. 1980); *In re Baksa*, 5 B.R. 184 (Bankr. N.D. Ohio 1980).

32. *Reeves*, 65 B.R. at 901-02 (Article 9 of the U.C.C. recognizes fixtures as personal property and security interest in fixtures as defined under Article 9 placed creditors outside of § 1322(b)(2) protection); *Secor Bank*, 129 B.R. at 465 (fixtures, along with security interest in escrowed funds for taxes, easements, mineral, oil, and water rights); *Caster*, 77 B.R. at 11-12 (fixtures, along with security interest in rents, profits, appliances, and furniture).

rights;³³ easements;³⁴ rents and profits;³⁵ stock;³⁶ life insurance policies;³⁷ commercial property on which debtors' happen to reside;³⁸ commercial property which was converted to a residence;³⁹ farmland on which the debtor happened to have his principal residence;⁴⁰ real property which included the debtor's principal residence and two rental units;⁴¹ irrigation equipment;⁴² machinery and equipment;⁴³ escrow accounts;⁴⁴ furniture;⁴⁵ appliances;⁴⁶ general household goods;⁴⁷ and automobiles.⁴⁸ A creditor, moreover, may not cancel its security interest in its additional collateral so as to gain § 1322(b)(2)'s protection where it has gained knowledge that a Chapter 13 petition and plan are being drafted by the debtor.⁴⁹

On the other hand, many courts have found the value of additional collateral to be illusory and that therefore the creditor's claim can be protected by the antimodification clause of § 1322(b)(2).⁵⁰ Liens found to be illusory include fixtures,⁵¹ general household goods,⁵² machinery and other equipment,⁵³

33. *Secor Bank*, 129 B.R. at 465.

34. *Id.*

35. *Hart*, 923 F.2d at 1415-16.

36. *Id.*

37. *Stiles*, 74 B.R. at 709-10; *Brantley*, 6 B.R. at 189-90.

38. *Foster*, 61 B.R. at 495.

39. *Hilderbran*, 54 B.R. at 586 (antimodification protection not afforded where debtors did not live on real property at time they cosigned mortgage; property was business at time of loan and was later converted to residence).

40. *Hines*, 64 B.R. at 686; *Leazier*, 55 B.R. at 871-72.

41. *Ramirez*, 62 B.R. at 670.

42. *Lapp*, 66 B.R. at 69.

43. *Wilson*, 895 F.2d at 128-29.

44. *Dent*, 130 B.R. at 628-30; *Secor Bank*, 129 B.R. at 465.

45. *Wilson*, 895 F.2d at 128-29; *Caster*, 77 B.R. at 11-12; *Baksa*, 5 B.R. at 186.

46. *Wilson*, 895 F.2d at 128-29.

47. *Kessler*, 99 B.R. at 637; *Johnson-Allen*, 67 B.R. at 976.

48. *Baksa*, 5 B.R. at 186.

49. *Id.* at 187.

50. As examples of cases holding that specific items did not constitute collateral separate from the debtor's principal residence, see, e.g., *Nobelman v. American Sav. Bank* (*In re Nobelman*), 129 B.R. 98 (N.D. Tex. 1991); *Wright v. C&S Family Credit, Inc.* (*In re Wright*), 128 B.R. 838 (Bankr. N.D. Ga. 1991); *In re Braylock*, 120 B.R. 61 (Bankr. N.D. Miss. 1990); *In re Diquinzio*, 110 B.R. 628 (Bankr. D.R.I. 1990); *In re Williams*, 109 B.R. 36 (Bankr. E.D.N.Y. 1989); *In re Ross*, 107 B.R. 759 (Bankr. W.D. Okla. 1989); *In re Hemsing*, 75 B.R. 689 (Bankr. D. Mont. 1987); *In re Foster*, 61 B.R. 492 (Bankr. N.D. Ind. 1986).

51. *Wright*, 128 B.R. at 843-44 (noting that under Georgia law, fixtures are part of realty and do not constitute separate security interest); *Williams*, 109 B.R. at 39 (holding that fixtures have nominal value).

52. *Williams*, 109 B.R. at 39 (holding that security interest in refrigerator, window

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insurance policies,⁵⁴ optional credit life coverage,⁵⁵ escrow funds,⁵⁶ rents and profits,⁵⁷ the common areas of a condominium complex,⁵⁸ an individual's guaranty of payment of a debtors' second mortgage,⁵⁹ and a security interest in a debtor's stock in the credit union with which the debtor made a loan.⁶⁰

Section 1322(b)(5)⁶¹ also provides a specific exception to § 1322(b)(2).⁶² Under § 1322(b)(5), a debtor may cure a default on a mortgage secured by her principal residence, deaccelerate, and reinstate the original terms of the mortgage obligation without modifying a creditor's rights in violation of § 1322(b)(2).⁶³

Other than the above exceptions, § 1322(b)(2) was initially construed to prevent any modification of a claim secured by real property which is the debtor's principal residence.⁶⁴ Specifically,

shades, and fixtures of nominal value do not constitute sufficient additional collateral to void antimodification protection).

53. *Ross*, 107 B.R. at 762 (common "boiler plate" language insufficient to void antimodification protection).

54. *Nobelman*, 129 B.R. at 104; *Wright*, 128 B.R. at 843-44 (right to premiums upon foreclosure is not a present security interest); *Ross*, 107 B.R. at 762.

55. *Braylock*, 120 B.R. at 63; *Diquinzio*, 110 B.R. at 629.

56. *Nobelman*, 129 B.R. at 104.

57. *Ross*, 107 B.R. at 762.

58. *Nobelman*, 129 B.R. at 104.

59. *Hemsing*, 75 B.R. at 691 (guaranty of payment is promise to pay money and not security within the definition of the Bankruptcy Code, where a security interest is defined as a charge against or interest in property).

60. *Foster*, 61 B.R. at 495 (holding that a security interest which a credit union held in a debtor's membership interest did not constitute additional security).

61. 11 U.S.C. § 1322(b)(5) (1988). The statute reads:

[N]otwithstanding paragraph (2) of this subsection, [the plan may] provide for the curing of any default within a reasonable time and maintenance of payments while the case is pending on any unsecured claim or secured claim on which the last payment is due after the date on which the final payment under the plan is due.

Id. 11 U.S.C. § 1322(b)(3) grants a more general protection by providing for the curing or waiving of any default. The text of § 1322(b)(3) states, "[The plan may] provide for the curing or waiving of any default." *Id.*

62. *See, e.g., Etchin v. Star Servs., Inc.*, 128 B.R. 662 (Bankr. W.D. Wisc. 1991) (section 1322(b)(5) is the "one and only" exception to § 1322(b)(2)). *But see In re Demoff*, 109 B.R. 902 (Bankr. N.D. Ind. 1989) (exceptions to § 1322(b)(2) besides § 1322(b)(5) do exist).

63. *Foster Mortgage Corp. v. Terry (In re Terry)*, 780 F.2d 894 (11th Cir. 1985). The *Terry* court noted that the Bankruptcy Code prohibition against modifying the rights of residential mortgage holders in § 1322(b)(2) is itself modified by § 1322(b)(5) which allows a debtor to modify the rights of a mortgagee by curing a default and reinstating regular installment payments. *Id.* at 896.

64. *Alexander L. Cataldo et al., Residential Mortgage Bifurcation Under Chapter 13*

mortgage lenders construed § 1322(b)(2) to prohibit any reduction in the value of their liens against debtors' homes through Chapter 13 bankruptcy.⁶⁵ In the last several years, however, debtors have increasingly utilized techniques to avoid lenders' liens against their homes.⁶⁶ The two primary techniques utilized in Chapter 13 to avoid lenders' liens against a home are commonly called "Chapter 20 Cramdown" and "Chapter 13 Cramdown."⁶⁷

II. CHAPTER 20 CRAMDOWN

A. Introduction

"Chapter 20" is a euphemism that describes the process of going through Chapter 7 bankruptcy and then again through Chapter 13.⁶⁸ Chapter 7 bankruptcy allows an individual to discharge her personal liability for a home mortgage.⁶⁹ The bank's right to proceed against her home *in rem*, however, survives the Chapter 7 bankruptcy.⁷⁰ Individuals who have gone through Chapter 7 bankruptcy, therefore, often file a subsequent petition under Chapter 13 to prevent *in rem* actions against their homes.⁷¹ With the subsequent filing, a debtor can receive protection against a creditor, including a stay against foreclosure actions, while making payments under a Chapter 13 plan to cure defaults of either the full or modified claims.⁷² Consequently, a

of the Bankruptcy Code, 96 COM. L.J. 225, 227-34 (1991); O'Reiley, *supra* note 20, at A1; Polk, *supra* note 11, at 281.

65. Polk, *supra* note 11, at 281.

66. See, e.g., *Johnson v. Home State Bank*, 111 S. Ct. 2150 (1991) (debtor filed Chapter 13 petition which sought to reinstate mortgage on which his personal liability had been discharged in a previous Chapter 7 case); *Eastland Mortgage Co. v. Hart (In re Hart)*, 923 F.2d 1410 (10th Cir. 1991) (in a Chapter 13 petition, debtor sought to strip undersecured mortgage lien to present value of property); *Wilson v. Commonwealth Mortgage Corp.*, 895 F.2d 123 (3d Cir. 1990); *Houghland v. Lomas & Nettleton Co.*, 886 F.2d 1182 (9th Cir. 1989); *Jim Walter Homes v. Saylors (In re Saylors)*, 869 F.2d 1434 (11th Cir. 1989).

67. See Polk, *supra* note 11, at 281-82; Carroll, *supra* note 30, at 882; Joann Henderson, *The Gaglia-Lowry Brief: A Quantum Leap from Strip Down to Chapter 7 Cram Down*, 8 BANKR. DEV. J. 131, at 173-80 (1991).

68. Henderson, *supra* note 67, at 173. *Johnson v. Home State Bank*, 111 S. Ct. 2150 (1991) (the United States Supreme Court ruled that Chapter 13 reorganization is not categorically foreclosed to a debtor who previously filed for Chapter 7 relief). See text accompanying notes 128 to 144.

69. See 11 U.S.C. § 524(a)(1) (1988); *Johnson*, 111 S.Ct. at 2153.

70. *Johnson*, 111 S. Ct. at 2152-53; Henderson, *supra* note 67, at 173.

71. Henderson, *supra* note 67, at 173.

72. H.R. REP. NO. 595, 95th Cong., 1st Sess. 118 (1977), reprinted in 1978

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debtor, through a Chapter 20 cramdown, may cure a default on a mortgage for which she no longer has personal liability; she has therefore modified the rights of a creditor in apparent violation of § 1322(b)(2).⁷³

The major issue arising in the Chapter 13 case is whether a mortgage lien securing an obligation for which a debtor's personal liability has been discharged in a Chapter 7 liquidation is a "claim" subject to inclusion in an approved Chapter 13 reorganization plan.⁷⁴ "Claim" is defined in § 101(5)⁷⁵ of the Bankruptcy Code as a "right to payment."⁷⁶ Courts disagree as to whether a lender has a right to payment against a mortgagor whose personal liability has been discharged in a previous Chapter 7 case.⁷⁷

B. The Minority View

Under the minority view, a Chapter 13 plan may not include a proposal to cure a default on a mortgage obligation that has previously been discharged in a Chapter 7 case.⁷⁸ Since the

U.S.C.C.A.N. 5963, 6079.

73. See *In re Russo*, 94 B.R. 127 (Bankr. N.D. Ill. 1988). The argument that a Chapter 20 cramdown impermissibly modifies the rights of a mortgagee in violation of § 1322(b)(2) is discussed *infra* at text accompanying notes 96 to 99.

74. *Johnson*, 111 S. Ct. at 2152.

75. 11 U.S.C. § 101(5) (Supp. III 1991). The statute reads:

"[C]laim" means—

(A) right to payment, whether or not such right is reduced to judgment, liquidated, unliquidated, fixed, contingent, matured, unmatured, disputed, undisputed, legal, equitable, secured, or unsecured; or

(B) right to an equitable remedy for breach of performance if such breach gives rise to a right to payment, whether or not such right to an equitable remedy is reduced to judgment, fixed, contingent, matured, unmatured, disputed, undisputed, secured, or unsecured.

Id.

76. *Id.*

77. The majority of decisions hold that a lender does have an enforceable obligation against the debtor and that this obligation is subject to restructuring in Chapter 13. See, e.g., *Jim Walter Homes, Inc. v. Saylor* (*In re Saylor*), 869 F.2d 1434 (11th Cir. 1989); *Downey Sav. & Loan Ass'n v. Metz* (*In re Metz*), 820 F.2d 1495 (9th Cir. 1987). Cases in which courts took the opposite view include *Home State Bank v. Johnson* (*In re Johnson*), 904 F.2d 563 (10th Cir. 1990), *rev'd*, 111 S. Ct. 2150 (1991); *In re Johnson*, 96 B.R. 326, 329 (D. Kan. 1989), *aff'd*, 904 F.2d 563 (10th Cir. 1990), *rev'd*, 111 S. Ct. 2150 (1991); *Grundy Nat'l Bank v. Johnson*, 106 B.R. 95 (W.D. Va. 1989).

78. As examples of cases adopting the minority view, see, e.g., *Home State Bank v. Johnson* (*In re Johnson*), 904 F.2d 563 (10th Cir. 1990) *rev'd*, 111 S. Ct. 2150 (1991); *In re Johnson*, 96 B.R. 326, 329 (D. Kan. 1989), *aff'd*, 904 F.2d 563 (10th Cir. 1990),

debtor has been discharged of personal liability in Chapter 7, the lender is no longer a "creditor" of the debtor and holds no claim against the debtor which could be included in the Chapter 13 plan.⁷⁹

Courts adopting the minority view have made several arguments in support of their decisions. One argument is that although the Bankruptcy Code does not expressly prohibit subsequent filings in Chapter 13, such filings were not intended by Congress.⁸⁰ As the Tenth Circuit stated: "While it is true that the Bankruptcy Code does not expressly prohibit [subsequent filings], we do not believe Congress intended such a result."⁸¹

A second argument is that although the Bankruptcy Code states that a "claim against the debtor" includes a claim against the property of the debtor,⁸² the legislative history indicates that such claims, or nonrecourse loans, must involve an "agreement" between the lender and the borrower.⁸³ Since the relationship between the lender and debtor was established by a bankruptcy proceeding, no agreement exists between them.⁸⁴ Without an agreement, the nonrecourse loan is not a "claim" for the purposes of the Bankruptcy Code.⁸⁵

rev'd, 111 S. Ct. 2150 (1991); *In re Russo*, 94 B.R. 127 (Bankr. N.D. Ill. 1988); *In re Reyes*, 59 B.R. 301 (Bankr. S.D. Cal. 1986); *In re McKinstry*, 56 B.R. 191 (Bankr. D. Vt. 1986); *In re Binford*, 53 B.R. 307 (Bankr. W.D. Ky. 1985); *In re Brown*, 52 B.R. 6 (Bankr. S.D. Ohio 1985); *Manufacturer's Hanover Mortgage Corp. v. Fryer* (*In re Fryer*), 47 B.R. 180 (Bankr. S.D. Ohio 1985).

79. See, e.g., *Home State Bank v. Johnson* (*In re Johnson*), 904 F.2d 563 (10th Cir. 1990), *rev'd*, 111 S. Ct. 2150 (1991); *In re Johnson*, 96 B.R. 326 (D. Kan. 1989), *aff'd*, 904 F.2d 563 (10th Cir. 1990), *rev'd*, 111 S. Ct. 2150 (1991); *In re Binford*, 53 B.R. 307 (Bankr. W.D. Ky. 1985); *In re Brown*, 52 B.R. 6 (Bankr. S.D. Ohio 1985).

80. *Home State Bank*, 904 F.2d at 565.

81. *Id.*

82. 11 U.S.C. § 102(2) (1988). The pertinent text of the statute reads: "claim against the debtor" includes a claim against property of the debtor. *Id.*

83. *Home State Bank*, 904 F.2d at 565. The Senate Report on the Bankruptcy Reform Act of 1978 states:

[Section 102(2)] is intended to cover nonrecourse loan agreements where the creditor's only rights are against property of the debtor, and not against the debtor personally. Thus, such an agreement would give rise to a claim that would be treated as a claim against the debtor personally.

S. REP. NO. 989, 95th Cong., 2d Sess. 28 (1978), reprinted in 1978 U.S.C.C.A.N. 5787, 5814.

84. *Home State Bank*, 904 F.2d at 566.

85. *Id.*; *Johnson*, 96 B.R. at 330.

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Third, courts adopting the minority view assert that the lender has no "claim" against the debtor as claim is defined under § 101(5)⁸⁶ because the lender has no "right to payment."⁸⁷ Since the debtor's personal liability was discharged in the previous Chapter 7 case, the lender has no right to payment from the debtor.⁸⁸ Similarly, courts adopting the minority view argue that the mortgagee is not a creditor as defined under § 101(10)⁸⁹ of the Bankruptcy Code and, hence, that they cannot be included in the Chapter 13 plan.⁹⁰

Fourth, courts adopting the minority view frown upon a debtor's attempt to reaffirm a mortgage in Chapter 13 after failing to do so in Chapter 7.⁹¹ As the court in *In re Ligon*⁹² expressed:

[A]n involuntary cure of the mortgage in a Chapter 13 case following discharge of personal liability on the mortgage in a Chapter 7 case without reaffirmation in effect forces the mortgagee to accept an involuntary reaffirmation in

86. 11 U.S.C. § 101(5) (Supp. III 1991). For the text of the statute, see *supra* note 75.

87. *Home State Bank*, 904 F.2d at 566; *Johnson*, 96 B.R. at 330; *Binford*, 53 B.R. at 309; *Brown*, 52 B.R. at 7.

88. *Home State Bank*, 904 F.2d at 566; *Johnson*, 96 B.R. at 330; *Binford*, 53 B.R. at 309; *Brown*, 52 B.R. at 7.

89. 11 U.S.C. § 101(10) (Supp. III 1991). The text of the statute reads:

"Creditor" means—

(A) entity that has a claim against the debtor that arose at the time of or before the order for relief concerning the debtor;

(B) entity that has a claim against the estate of a kind specified in section 348(d), 502(f), 502(g), 502(h) or 502(i) of this title; or

(C) entity that has a community claim.

Id.

90. *McKinstry*, 56 B.R. at 193.

91. *Johnson*, 96 B.R. at 330; *Binford*, 53 B.R. at 309; *Brown*, 52 B.R. at 7.

92. 97 B.R. 398 (Bankr. N.D. Ill. 1989). The *Ligon* court, however, ultimately rejected this argument.

93. 11 U.S.C. § 524(c) (1988). The statute reads:

An agreement between a holder of a claim and the debtor, the consideration for which, in whole or in part, is based on a debt that is dischargeable in a case under this title is enforceable under applicable nonbankruptcy law, whether or not discharge is waived, only if—

(1) such agreement was made before the granting of the discharge under section 727, 1141, 1228, or 1328 of this title;

(2) such agreement contains a clear and conspicuous statement which advises the debtor that the agreement may be rescinded at any time prior to discharge or within sixty days after such agreement is filed with the court, whichever occurs later, by giving notice of rescission to the holder of such claim;

contradiction of the policy found in [sections] 524(c)⁹³ and [524](d)⁹⁴ of the Bankruptcy Code.⁹⁵

(3) such agreement has been filed with the court and, if applicable, accompanied by a declaration or an affidavit of the attorney that represented the debtor during the course of negotiating an agreement under this subsection, which states that such agreement—

(A) represents a fully informed and voluntary agreement by the debtor; and

(B) does not impose an undue hardship on the debtor or a dependent of the debtor;

(4) the debtor has not rescinded such agreement at any time prior to discharge or within sixty days after such agreement is filed with the court, whichever occurs later, by giving notice of rescission (sic) to the holder of such claim;

(5) the provisions of subsection (d) of this section have been complied with; and

(6)(A) in a case concerning an individual who was not represented by an attorney during the course of negotiating an agreement under this subsection, the court approves such agreement as—

(i) not imposing an undue hardship on the debtor or a dependent of the debtor; and

(ii) in the best interest of the debtor.

(B) Subparagraph (A) shall not apply to the extent that such debt is a consumer debt secured by real property.

Id.

94. 11 U.S.C. § 524(d) (1988). The statute reads:

In a case concerning an individual, when the court has determined whether to grant or not to grant a discharge under section 727, 1141, 1228, or 1328 of this title, the court may hold a hearing at which the debtor shall appear in person. At any such hearing, the court shall inform the debtor that a discharge has been granted or the reason why a discharge has not been granted. If a discharge has been granted and if the debtor desires to make an agreement of the kind specified in subsection (c) of this section, then the court shall hold a hearing at which the debtor shall appear in person and at such hearing the court shall—

(1) inform the debtor—

(A) that such an agreement is not required under this title, under nonbankruptcy law, or under any agreement not made in accordance with the provisions of subsection (c) of this section; and

(B) of the legal effect and consequences of—

(i) an agreement of the kind specified in subsection (c) of this section; and

(ii) a default under such an agreement;

(2) determining whether the agreement that the debtor desires to make complies with the requirements of subsection (c)(6) of this section, if the consideration for such agreement is based in whole or in part on a consumer debt that is not secured by real property of the debtor.

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Finally, courts adopting the minority view argue that allowing a Chapter 13 debtor to include a mortgage debt that has been discharged in a previous Chapter 7 case would impermissibly modify the rights of a lender whose claim was secured by the debtor's principal residence.⁹⁶ When the personal liability of the debtor has been discharged in Chapter 7, reinstatement of the mortgage would create a new debt arrangement between the debtor and the mortgagee.⁹⁷ Under such an arrangement, the lender's only recourse would be against the property; such a limited right would be a significant modification of the rights of the lender in violation of § 1322(b)(2).⁹⁸ Consequently, § 1322(b)(2) prevents a debtor from curing and reinstating only the secured portion of the mortgagee's claim.⁹⁹

C. *The Majority View*

Under the majority view, a Chapter 13 plan may cure a home mortgage arrearage after the debtor has received a Chapter 7 discharge of personal liability for the mortgage debt.¹⁰⁰ Generally, courts adopting the majority view assert that the debt owed by the mortgagor is transformed into a nonrecourse obligation at the time of the Chapter 7 discharge and that a nonrecourse debt may be cured in a Chapter 13 plan.¹⁰¹

Courts adopting the majority view justify their position with several arguments. First, they note that there is no statutory prohibition against the inclusion of a mortgage debt which was previously discharged under Chapter 7 except the § 1325(a)(3)¹⁰² requirement of good faith.¹⁰³ Under § 1325,¹⁰⁴

Id.

95. *Ligon*, 97 B.R. at 402.

96. *In re Russo*, 94 B.R. 127, 128 (Bankr. N.D. Ill. 1988).

97. *Id.*

98. *Id.*

99. *Id.*

100. As examples of cases adopting the majority view, see, e.g., *Jim Walter Homes, Inc. v. Saylor* (*In re Saylor*), 869 F.2d 1434 (11th Cir. 1989); *Downey Sav. & Loan Ass'n v. Metz* (*In re Metz*), 820 F.2d 1495 (9th Cir. 1987); *Grundy Nat'l Bank v. Johnson*, 106 B.R. 95 (W.D. Va. 1989); *In re Ligon*, 97 B.R. 398 (Bankr. N.D. Ill. 1989); *Federal Land Bank v. Smith* (*In re Smith*), 94 B.R. 216 (Bankr. M.D. Ga. 1988); *In re Hagberg*, 92 B.R. 809 (Bankr. W.D. Wis. 1988); *In re Klapp*, 80 B.R. 540 (Bankr. W.D. Okla. 1987); *In re Lagasse*, 66 B.R. 41 (Bankr. D. Conn. 1986); *In re Lewis*, 63 B.R. 90 (Bankr. E.D. Pa. 1986).

101. See, e.g., *Saylor*, 869 F.2d at 1436; *Metz*, 820 F.2d at 1498; *Grundy Nat'l Bank*, 106 B.R. at 98; *Hagberg*, 92 B.R. at 812.

102. 11 U.S.C. § 1325(a)(3) (1988). The text of the statute reads: [The court shall

the Chapter 13 court is required to confirm the debtor's plan so long as it meets the technical requirements of the Code, is feasible, and is proposed in good faith.¹⁰⁵ The *Saylors* court reasons that "[t]he good faith requirement of § 1325(a)(3) is sufficient to prevent *undeserving* debtors from using this procedure [Chapter 20 cramdown], yet does not also prevent *deserving* debtors from using the procedure."¹⁰⁶

Secondly, they note that, as defined under § 102(2),¹⁰⁷ a "claim against a debtor" includes a claim against the property of the debtor.¹⁰⁸ Since the lender still has a claim against property of the debtor after Chapter 7, he still has a claim subject to a Chapter 13 plan.¹⁰⁹ Other courts adopting the majority view argue that the remaining debt of the Chapter 13 petitioner is a nonrecourse loan obligation that can permissibly be included in

confirm a Chapter 13 plan if] the plan has been proposed in good faith and not by any means forbidden by law. *Id.*

103. *Saylors*, 869 F.2d at 1436; *Metz*, 820 F.2d at 1498; *Lagasse*, 66 B.R. at 43.

104. 11 U.S.C. § 1325 (1988). Section 1325 provides the conditions for confirmation of a Chapter 13 plan. The statute reads in relevant part:

(a) Except as provided in subsection (b), the court shall confirm a plan if—

(1) The plan complies with the provisions of this chapter and with other applicable provisions of this title

. . . .

(3) the plan has been proposed in good faith and not by any means forbidden by law

. . . .

(6) the debtor will be able to make all payments under the plan and to comply with the plan.

Id. Subsection (b) provides conditions under which a plan may be confirmed despite objections by the trustee or a holder of an allowed unsecured claim. *Id.*

105. *Id.*

106. *Saylors*, 869 F.2d at 1436 (emphasis added).

107. 11 U.S.C. § 102(2) (1988). For the text of this statute, see *supra* note 82.

108. *Saylors*, 869 F.2d at 1436; *Hagberg*, 92 B.R. at 814. Interestingly, these courts cite to legislative history similar to that offered by the minority view but find no limitation due to the "agreement" language of the legislative history. *Hagberg*, 92 B.R. at 814 (citing S. REP. NO. 989, 95th Cong., 2d Sess. 28 (1978), *reprinted in* 1978 U.S.C.C.A.N. 5787, 5814); *Saylors*, 869 F.2d at 1436 (citing H.R. REP. NO. 595, 95th Cong., 1st Sess. 315 (1977), *reprinted in* 1978 U.S.C.C.A.N. 5963, 6272). The House Report states in pertinent part:

[Section 102(2)] specifies that "claim against the debtor" includes claim against property of the debtor. This paragraph is intended to cover nonrecourse loan agreements where the creditor's only rights are against property of the debtor, and not against the debtor personally.

H.R. REP. NO. 595, 95th Cong., 1st Sess. 315 (1977), *reprinted in* 1978 U.S.C.C.A.N. 5963, 6272. For the text of the Senate report, see *supra* note 83.

109. *Saylors*, 869 F.2d at 1436; *Grundy Nat'l Bank*, 106 B.R. at 98.

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the Chapter 13 plan.¹¹⁰ Recognizing the minority view that a nonrecourse loan cannot be included because it is not consensual, the courts adopting the majority view note that § 102(2) is “not limited to consensual nonrecourse lien claims. It refers to any claim against the debtor’s property in its definition of claims against the debtor.”¹¹¹ Consequently, regardless of whether the mortgagee’s lien is consensual or nonconsensual, it is still a “claim” that can be included in a Chapter 13 plan.¹¹² Thus, the ultimate position of the courts adopting the majority view is that “all legal obligations of the debtor are claims.”¹¹³

Finally, courts adopting the majority view do not read § 1322(b)(2) to prohibit Chapter 20 cramdown of home mortgages.¹¹⁴ They reason that although § 1322(b)(2) does not allow a debtor to “modify” a claim secured by a security interest in a debtor’s principal residence, § 1322(b)(3)¹¹⁵ allows debtors to “cure” “any default.”¹¹⁶ Since the Chapter 13 petition only seeks to cure a default, no impermissible modification occurs.¹¹⁷

D. Johnson v. Home State Bank

1. History of the Case

The Supreme Court of the United States, in *Johnson v. Home State Bank*,¹¹⁸ resolved the dispute over whether a debtor may resort to Chapter 13 after previously having a debt discharged under Chapter 7. The Court held that Chapter 13 reorganization is not categorically closed to a debtor who previously filed for Chapter 7 relief.¹¹⁹ Johnson, the debtor, defaulted on promissory notes secured by a mortgage on his farm.¹²⁰ Home State Bank thereafter began foreclosure proceedings in state court.¹²¹ Johnson filed for liquidation under Chapter 7 and the bankruptcy court discharged him from personal liability on the

110. *Ligon*, 97 B.R. at 402; *Lagasse*, 66 B.R. at 43.

111. *Ligon*, 97 B.R. at 402.

112. *Id.* at 402-03.

113. *Lewis*, 63 B.R. at 92.

114. *Metz*, 820 F.2d at 1497.

115. 11 U.S.C. § 1322(b)(3) (1988). For the text of this statute, see *supra* note 61.

116. *Metz*, 820 F.2d at 1497.

117. *Id.*

118. 111 S. Ct. 2150 (1991).

119. *Id.*

120. *Id.*

121. *Id.*

notes.¹²² After the stay protecting Johnson's estate was lifted, the bank reinstated proceedings against his estate *in rem*.¹²³ After the state court entered judgment for the bank, but before the foreclosure sale, Johnson filed for protection under Chapter 13.¹²⁴ The bankruptcy court confirmed his plan.¹²⁵ The district court reversed, holding that bankruptcy law does not protect a debtor under Chapter 13 whose personal liability has been discharged under Chapter 7.¹²⁶ The Tenth Circuit affirmed, holding that the bank no longer had a "claim" against the petitioner subject to rescheduling under Chapter 13.¹²⁷

2. *The View of the United States Supreme Court*

The Supreme Court of the United States reversed, holding that a claim subject to rescheduling under Chapter 13 survived Johnson's Chapter 7 liquidation.¹²⁸ The Court unanimously agreed that a mortgage lien securing an obligation for which a debtor's personal liability has been discharged in a Chapter 7 liquidation is a "claim" within the meaning of § 101(5)¹²⁹ and is subject to inclusion in an approved Chapter 13 reorganization plan. The Court explained that Congress intended to adopt the broadest possible definition of "claim."¹³⁰ A claim, as defined under § 101(5), means "right to payment" and "right to equitable remedy"; these terms mean "nothing more nor less than an enforceable obligation."¹³¹ A mortgage interest that survives

122. *Id.*

123. *Id.*

124. *Id.*

125. *Id.*

126. *In re Johnson*, 96 B.R. 326 (D. Kan. 1989), *aff'd*, 904 F.2d 563 (10th Cir. 1990), *rev'd*, 111 S. Ct. 2150 (1991).

127. *Home State Bank v. Johnson (In re Johnson)*, 904 F.2d 563 (10th Cir. 1990), *rev'd*, 111 S. Ct. 2150 (1991).

128. *Johnson v. Home State Bank*, 111 S. Ct. 2150 (1991).

129. 11 U.S.C. § 101(5) (1988). For the text of this statute, see *supra* note 75.

130. *Johnson*, 111 S. Ct. at 2154 (citing *Pennsylvania Dep't of Pub. Welfare v. Davenport*, 495 U.S. 552, 558 (1990)). *Davenport* held that "Congress chose expansive language" reflecting "Congress' broad rather than restrictive view of the class of obligations that qualify as a 'claim.'" *Id.* The court elaborated, stating that the intended definition of "claim" was the "broadest possible" and that it "contemplates that all legal obligations of the debtor . . . will be able to be dealt with in the bankruptcy case." *Id.* (citing H.R. REP. NO. 595, 95th Cong., 1st Sess. 309 (1977), *reprinted in* 1978 U.S.C.C.A.N. 5963, 6266).

131. *Johnson*, 111 S. Ct. at 2154 (citing *Davenport*, 495 U.S. at 558).

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Chapter 7 is an “enforceable obligation” of the debtor.¹³² As the Court stated: “[E]ven after the debtor’s personal obligations have been extinguished, the mortgage holder still retains a ‘right to payment’ in the form of its right to the proceeds from the sale of the debtor’s property.”¹³³ Alternatively, the creditor’s right to foreclose on the debtor’s property after the Chapter 7 discharge can be viewed as a “right to an equitable remedy” for the debtor’s default on the underlying obligation.¹³⁴

The Court also noted that § 502(b)(1)¹³⁵ recognizes that a “claim” may consist of nothing more than an obligation that is enforceable against a debtor’s property.¹³⁶ Similarly, § 102(2) establishes that a “claim against a debtor” includes a “claim against property of the debtor.”¹³⁷ The Court also rejected the Bank’s claim that serial filings under Chapter 7 and Chapter 13 evaded Congressional intent since Congress had expressly prohibited various forms of serial filings¹³⁸ but placed no restrictions with regard to Chapter 7 and Chapter 13.¹³⁹ Finally, the Court stated that Congress did not intend to use the Code’s definition of “claim” to police the Chapter 13 process for abuse.¹⁴⁰

The Supreme Court remanded the case, leaving two other issues to be decided by the lower courts. The Court noted that the issues of “good faith”¹⁴¹ and “feasibility”¹⁴² still needed to

132. *Id.*

133. *Id.*

134. *Id.*

135. 11 U.S.C. § 502(b)(1) (1988). The statute reads:

[s]uch claim is unenforceable against the debtor and property of the debtor, under any agreement or applicable law for a reason other than because such claim is contingent or unmatured.

Id.

136. *Johnson*, 111 S. Ct. at 2155.

137. *Id.*

138. *Id.* at 2156. The court noted that 11 U.S.C. § 109(g) allowed no filings within 180 days of dismissal, § 727(a)(8) allowed no Chapter 7 filing within 6 years of a Chapter 7 or Chapter 11 filing, and § 727(a)(9) limits Chapter 7 filing within 6 years of Chapter 12 or Chapter 13 filing. *Id.* The Court stated:

The absence of a like prohibition on serial filings of Chapter 7 and Chapter 13 petitions, combined with the evident care with which Congress fashioned these express prohibitions, convinces us that Congress did not intend categorically to foreclose the benefit of Chapter 13 reorganization to a debtor who previously has filed for Chapter 7 relief.

Id.

139. *Id.*

140. *Id.*

141. 11 U.S.C. § 1325(a)(3) (1988). The general rule for judging good faith is a

be addressed.¹⁴³ Since neither issue was considered in the lower courts, they were left to be considered on remand.¹⁴⁴

E. After Johnson v. Home State Bank

The Supreme Court's decision in *Johnson* established that a mortgage lien which survives a Chapter 7 discharge of the debtor's personal liability on the underlying note qualifies as a "claim" against the mortgagors and is subject to treatment in a subsequent Chapter 13 case.¹⁴⁵ The second petition must still meet the requirements for a Chapter 13 petition.¹⁴⁶ As the *Johnson* Court indicated, two of these requirements are the requirements of "good faith" and "feasibility" under § 1325(a).¹⁴⁷ Moreover, claims involving mortgage liens face at least one

"totality of the circumstances" test. *Downy Sav. & Loan Ass'n v. Metz (In re Metz)*, 820 F.2d 1495, 1498 (9th Cir. 1987). The Eleventh Circuit has established a list of factors to be considered by bankruptcy courts in their determinations of a debtor's good faith in proposing a Chapter 13 plan. *Kitchens v. Georgia R.R. Bank and Trust Co. (In re Kitchens)*, 702 F.2d 885, 888-89 (11th Cir. 1983). As the *Kitchens* court stated:

[A] bankruptcy court must consider but [is not] limited to the following:

- (1) the amount of the debtor's income from all sources;
- (2) the living expenses of the debtor and his dependents;
- (3) the amount of attorney's fees;
- (4) the probable or expected duration of the debtor's Chapter 13 plan;
- (5) the motivations of the debtor and his sincerity in seeking relief under the provisions of Chapter 13;
- (6) the debtor's degree of effort;
- (7) the debtor's ability to earn and the likelihood of fluctuation in his earnings;
- (8) special circumstances such as inordinate medical expense;
- (9) the frequency with which the debtor has sought relief under the Bankruptcy Reform Act and its predecessors;
- (10) the circumstances under which the debtor has contracted his debts and his demonstrated bona fides, or lack of same, in dealing with creditors; [and]
- (11) the burden which the plan's administration would place on the trustee.

Id. The *Kitchens* court also recognized a hardship factor, holding that "other factors or exceptional circumstances may support a finding of good faith." *Id.* at 889.

142. 11 U.S.C. § 1325(a)(6) (1988). The feasibility issue involves the debtor's ability to make the payments as provided in her plan. *Id.*

143. *Johnson*, 111 S. Ct. at 2156.

144. *Id.*

145. *Johnson v. Home State Bank*, 111 S. Ct. 2150 (1991).

146. See, e.g., *id.* at 2156; *Secor Bank v. Dunlap*, 129 B.R. 463, 465 (D. La. 1991).

147. *Johnson*, 111 S. Ct. at 2156; see *supra* notes 141-44 and accompanying text.

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additional requirement: the antimodification requirement of § 1322(b)(2).¹⁴⁸

III. TRADITIONAL INTERPRETATIONS OF CHAPTER 13 CRAMDOWN

A. Introduction

Chapter 13 cramdown involves the reduction of a debt to the present value of the collateral securing that debt.¹⁴⁹ In a Chapter 13 cramdown of a residential mortgage, an individual attempts to have the value of her mortgage reduced to the value of her home pursuant to § 506(a)¹⁵⁰ of the Bankruptcy Code.¹⁵¹ Section 506(a) allows an individual to bifurcate an undersecured lien into two claims: a "secured" claim equaling the market value of the collateral and an "unsecured" claim to the extent of the lien's value beyond the value of the collateral.¹⁵² The issue in Chapter 13 cramdown is whether this provision of general applicability applies to real property which is the debtor's principal residence, which is specifically afforded special protection under § 1322(b)(2).¹⁵³

148. See, e.g., *Secor Bank*, 129 B.R. at 465. For a discussion of the antimodification clause of § 1322(b)(2), see *supra* notes 9-18 and accompanying text.

149. See 11 U.S.C. §§ 506(a), 1322(b)(2), and 1325(a) (1988); see also Cataldo, *supra* note 64, at 226.

150. 11 U.S.C. § 506(a) (1988). The statute reads in relevant part:

An allowed claim of a creditor secured by a lien on property in which the estate has an interest . . . is a secured claim to the extent of the value of such creditor's interest in such property . . . and is an unsecured claim to the extent that the value of such creditor's interest . . . is less than the amount of such allowed claim.

Id. For the text of the statute, see *supra* note 23.

151. As examples of cases where a debtor tried to have the value of her mortgage reduced to the present value of her home pursuant to § 506(a), see, e.g., *Eastland Mortgage Co. v. Hart* (*In re Hart*), 923 F.2d 1410 (10th Cir. 1991); *Wilson v. Commonwealth Mortgage Corp.*, 895 F.2d 123 (3d Cir. 1990); *Houghland v. Lomas & Nettleton Co.* (*In re Houghland*), 886 F.2d 1182 (9th Cir. 1989); *Wright v. C&S Family Credit, Inc.* (*In re Wright*), 128 B.R. 838 (Bankr. N.D. Ga. 1991); *In re Chavez*, 117 B.R. 733 (Bankr. S.D. Fla. 1990); *In re Harris*, 94 B.R. 832 (D.N.J. 1989); *In re Russell*, 93 B.R. 703 (D.N.D. 1988).

152. 11 U.S.C. § 506(a) (1988).

153. As examples of cases discussing the applicability to a debtor's principal residence of § 506(a) in Chapter 13 petitions, see, e.g., *Eastland Mortgage Co. v. Hart* (*In re Hart*), 923 F.2d 1410 (10th Cir. 1991); *Wilson v. Commonwealth Mortgage Corp.*, 895 F.2d 123 (3d Cir. 1990); *Houghland v. Lomas & Nettleton Co.* (*In re Houghland*), 886 F.2d 1182 (9th Cir. 1989); *Wright v. C&S Family Credit, Inc.* (*In re Wright*), 128 B.R. 838 (Bankr. N.D. Ga. 1991); *In re Chavez*, 117 B.R. 733 (Bankr. S.D. Fla. 1990); *In re Harris*, 94 B.R. 832 (D.N.J. 1989); *In re Russell*, 93 B.R. 703

B. *The Minority View*

The minority view holds that § 1322(b)(2) requires allowance of a claim secured only by a security interest in the debtor's principal residence for the entire balance owed on such debt, regardless of the value of the collateral.¹⁵⁴ Several arguments support this position. First, courts adopting the minority view contend that the plain meaning of the statute affords protection to holders of claims secured by a debtor's principal residence.¹⁵⁵ "The clearly focused concern is with the rights of *holders* of residential real estate mortgages;" the statute grants rights to holders of mortgage claims.¹⁵⁶ Thus, the "straight-forward, common-sense reading" of § 1322(b)(2) compels denial of the application of § 506(a) since it would modify the rights of mortgagees in violation of § 1322(b)(2).¹⁵⁷

Secondly, courts adopting the minority view argue that bifurcation would defeat the Congressional intent behind § 1322(b)(2).¹⁵⁸ Courts adopting the minority view assert that Congress intended "to protect residential mortgagees in Chapter 13 cases by prohibiting any modification of the mortgagee's secured lien with the sole exception of curing a default and reinstating the regular payments both of which are specifically allowed under § 1322(b)(5)."¹⁵⁹ Consequently, "the use of § 506

(D.N.D. 1988); Polk, *supra* note 11, at 281-83; Carroll, *supra* note 30, at 881; Cataldo, *supra* note 64, at 227-40.

154. As examples of cases adopting the minority view, see e.g., Nobelman v. American Sav. Bank (*In re Nobelman*), 129 B.R. 98 (N.D. Tex. 1991); Etchin v. Star Servs., Inc. (*In re Etchin*), 128 B.R. 662 (Bankr. W.D. Wis. 1991); First Interstate Bank v. Woodall (*In re Woodall*), 123 B.R. 95 (W.D. Okla. 1990), *rev'd*, 931 F.2d 62 (10th Cir. 1991); *In re Moran*, 121 B.R. 879 (Bankr. E.D. Okla. 1990); *In re Chavez*, 117 B.R. 733 (Bankr. S.D. Fla. 1990); *In re Sauber*, 115 B.R. 197 (Bankr. D. Minn. 1990); *In re Schum*, 112 B.R. 159 (Bankr. N.D. Tex. 1990); *In re Kaczmarczyk*, 107 B.R. 200 (Bankr. D. Neb. 1989); *In re Russell*, 93 B.R. 703 (D.N.D. 1988); *In re Brown*, 91 B.R. 19 (Bankr. E.D. Va. 1988); *In re Catlin*, 81 B.R. 522 (Bankr. D. Minn. 1987); *In re Hemsing*, 75 B.R. 689 (Bankr. D. Mont. 1987); *In re Hynson*, 66 B.R. 246 (Bankr. D.N.J. 1986), *overruled by In re Harris*, 94 B.R. 832 (D.N.J. 1989); *In re Smith*, 63 B.R. 15 (Bankr. D.N.J. 1986).

155. Nobelman, 129 B.R. at 104; Sauber, 115 B.R. at 199; Schum, 112 B.R. at 162; Russell, 93 B.R. at 705; Hynson, 66 B.R. at 252.

156. Sauber, 115 B.R. at 199 (emphasis added).

157. *Id.*

158. Moran, 121 B.R. at 882-83; Chavez, 117 B.R. at 736; Schum, 112 B.R. at 162; Hemsing, 75 B.R. at 692; Hynson, 66 B.R. at 252.

159. Chavez, 117 B.R. at 736.

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in a Chapter 13 results in a benefit" which was not the "intent of the framers of the Bankruptcy Code."¹⁶⁰

Third, courts adopting the minority view argue that the historical context of Chapter 13 indicates that the modification of mortgage liens is impermissible.¹⁶¹ Under the Bankruptcy Code:

[L]ike its predecessor [in the Bankruptcy Act], Chapter 13 maintains a distinction between claims secured by certain real property and claims secured by other collateral. Under Chapter XIII, a claim secured by real property could not be dealt with under the plan This basic rule has continued except as explicitly changed by the Bankruptcy Code § 1322(b)(2) continued the prohibition on modifying the rights of holders of claims secured by real estate, but only with respect to real estate that constitutes the debtor's principal residence. If Congress has intended to change the manner in which a claim secured by a debtor's residence would be treated under the Code it would have specifically limited § 1322(b)(2) to claims secured pursuant to § 506. However, as Congress did not explicitly change the treatment of claims secured by a mortgage on a debtor's residence . . . a continuity of treatment of such claims was intended.¹⁶²

Fourth, because a basic rule of statutory construction provides that where two statutes conflict, the specific will prevail over the general; many courts adopting the minority view assert that the specific language of § 1322(b)(2) prevails over the general language of § 506(a).¹⁶³ As the *Nobelman* court states, "an inescapable, although limited, conflict" between the sections exists.¹⁶⁴ Since it is "clear" that § 506 can be used to "undermine the protection afforded by section 1322(b)(2)," the specific language of § 1322(b)(2) prevails, and bifurcation is denied.¹⁶⁵

Fifth, courts adopting the minority view note that the § 1322(b)(2) exemption applies to a "claim" secured by a security

160. *Moran*, 121 B.R. at 883.

161. *Moran*, 121 B.R. at 882; *Kaczmarczyk*, 107 B.R. at 202-03.

162. *Kaczmarczyk*, 107 B.R. at 203.

163. *Nobelman*, 129 B.R. at 102; *Moran*, 121 B.R. at 882; *Chavez*, 117 B.R. at 735; *Russell*, 93 B.R. at 706; *Catlin*, 81 B.R. at 524; *Hemsing*, 75 B.R. at 691-92; *Hynson*, 66 B.R. at 249; *Smith*, 63 B.R. at 18.

164. *Nobelman*, 129 B.R. at 102 n.2.

165. *Id.* at 102.

interest in debtor's principal residence and not a "secured claim."¹⁶⁶ As the *Hynson* court argues:

The concept that only a "secured claim" . . . of a mortgagee is protected within the ambit of § 1322(b)(2) carries the syntax of the Bankruptcy Code to an absurd conclusion which is at odds with the general principles of statutory construction and with the clear legislative intent of § 1322(b)(2). This court notes that § 1322(b)(2) protects "a claim secured only by a security interest in real property that is the debtor's principal residence." The language of § 1322(b)(2) does not specifically limit its protection to a *secured* claim secured only by a security interest in such real property [T]he emphasis in determining the applicability of § 1322(b)(2) should be on the existence of a claim, which is a right to payment.¹⁶⁷

Finally, courts adopting the minority view argue that the bifurcation of the mortgagees' claims would vitiate the protection of § 1322(b)(2).¹⁶⁸ As the *Smith* court reasons:

[Bifurcation] leaves section 1322(b)(2) without any *raison d'être*. "Cramdown" presupposes that a secured creditor will retain its lien and that its rights will be modified if it is undersecured. If the claim is no longer secured under section 506(a), and section 1322(b)(2) does not apply, the exception for debtor's principal residence is unnecessary. A statute should not be interpreted so as to leave it with no meaning whatsoever.¹⁶⁹

C. The Majority View

Under the majority view, a Chapter 13 plan that bifurcates an undersecured claim into secured and unsecured claims pursuant to § 506(a) does not violate the protection afforded lenders under § 1322(b)(2).¹⁷⁰ The courts adopting the majority view assert

166. *Moran*, 121 B.R. at 882; *Russell*, 93 B.R. at 706; *Hemsing*, 75 B.R. at 692; *Hynson*, 66 B.R. at 253.

167. *Hynson*, 66 B.R. at 253 (emphasis added).

168. *Nobelman*, 129 B.R. at 102; *Moran*, 121 B.R. at 882; *Sauber*, 115 B.R. at 199; *Hynson*, 66 B.R. at 252; *Smith*, 63 B.R. at 16.

169. *Smith*, 63 B.R. at 16 (emphasis added).

170. As examples of courts adopting the majority view, see e.g., *Eastland Mortgage Co. v. Hart* (*In re Hart*), 923 F.2d 1410 (10th Cir. 1991); *Wilson v. Commonwealth Mortgage Corp.*, 895 F.2d 123 (3d Cir. 1990); *Houghland v. Lomas & Nettleton Co.* (*In re Houghland*), 886 F.2d 1182 (9th Cir. 1989); *In re Ward*, 129 B.R. 664 (Bankr. W.D. Okla. 1991); *Secor Bank v. Dunlap*, 129 B.R. 463 (E.D. La. 1991); *Wright v.*

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that bifurcation does not constitute a modification but rather is a recognition of the legal status of the creditor's interest in the debtor's property.¹⁷¹ As the Tenth Circuit stated, "an undersecured mortgage is, for the purposes of the bankruptcy code, two *claims*, and only the secured *claim* is protected by section 1322(b)(2)."¹⁷²

The courts adopting the majority view offer several reasons for their decisions. First, they argue that the antimodification clause refers to secured claims.¹⁷³ Section 1322(b)(2) reads, "[the plan may] modify the rights of holders of secured claims, other than a claim secured only by a security interest in real property that is the debtor's principal residence, or of holders of unsecured claims."¹⁷⁴ Given the syntax of this clause, the courts adopting the majority view read the word "claim" in the antimodification clause to refer back to "secured claims."¹⁷⁵ The *Simmons* court, for example, contends that it cannot "ignore the clause immediately preceding [the antimodification clause] that states: 'modify the rights of holders of *secured claims*.' This court must interpret this clause as specifically limiting the section 1322(b)(2)

C&S Family Credit, Inc. (*In re Wright*), 128 B.R. 838 (Bankr. N.D. Ga. 1991); *In re Honett*, 116 B.R. 495 (Bankr. E.D. Tex. 1990); *McNair v. Chrysler First Fin. Servs. Corp.* (*In re McNair*), 115 B.R. 520 (Bankr. E.D. Va. 1990); *In re Gadson*, 114 B.R. 453 (Bankr. E.D. Va. 1990); *In re Diquinzio*, 110 B.R. 628 (Bankr. D.R.I. 1990); *Brouse v. CSB Mortgage Corp.* (*In re Brouse*), 110 B.R. 539 (Bankr. D. Colo. 1990); *In re Demoff*, 109 B.R. 902 (Bankr. N.D. Ind. 1989); *In re Ross*, 107 B.R. 759 (Bankr. W.D. Okla. 1989); *Kessler v. Homestead Sav.* (*In re Kessler*), 99 B.R. 635 (Bankr. E.D. Pa. 1989); *In re Hill*, 96 B.R. 809 (Bankr. S.D. Ohio 1989); *In re Frost*, 96 B.R. 804 (Bankr. S.D. Ohio 1989), *aff'd*, 123 B.R. 254 (S.D. Ohio 1990); *In re Harris*, 94 B.R. 832 (D.N.J. 1989); *Kehm v. Citicorp Homeowners Serv., Inc.* (*In re Kehm*), 90 B.R. 117 (Bankr. E.D. Pa. 1988); *In re Shaffer*, 84 B.R. 63 (Bankr. W.D. Va. 1988), *aff'd sub nom.* Capital Credit Plan v. Shaffer, 116 B.R. 60 (W.D. Va. 1988); *In re Simmons*, 78 B.R. 300 (Bankr. D. Kan. 1987); *Caster v. United States* (*In re Caster*), 77 B.R. 8 (Bankr. E.D. Pa. 1987); *Cameron Brown Co. v. Bruce* (*In re Bruce*), 40 B.R. 884 (Bankr. W.D. Va. 1984); *Spadel v. Household Consumer Discount Co* (*In re Spadel*), 28 B.R. 537 (Bankr. E.D. Pa. 1983); *In re Neal*, 10 B.R. 535 (Bankr. S.D. Ohio 1981).

171. See, e.g., *Hart*, 923 F.2d at 1411.

172. *Id.* at 1415 (emphasis added).

173. *Wilson*, 895 F.2d at 127; *Houghland*, 886 F.2d at 1184; *Demoff*, 109 B.R. at 919; *Frost*, 96 B.R. at 807; *Harris*, 94 B.R. at 836; *Kehm*, 90 B.R. at 120; *Simmons*, 78 B.R. at 303.

174. 11 U.S.C. § 1322(b)(2) (1988).

175. *Wilson*, 895 F.2d at 127; *Houghland*, 886 F.2d at 1184; *Demoff*, 109 B.R. at 919; *Frost*, 96 B.R. at 807; *Harris*, 94 B.R. at 836; *Kehm*, 90 B.R. at 120; *Simmons*, 78 B.R. at 303.

protection to fully secured claims."¹⁷⁶ Consequently, the antimodification clause limits modification only of that portion of the claim that is secured.¹⁷⁷

Second, other courts have framed a similar argument. They argue that § 506 provides the process by which the determination of whether a claim is secured under § 1322(b)(2) is made.¹⁷⁸ In making this argument, courts adopting the majority view cite the Supreme Court's ruling in *United States v. Ron Pair Enterprises*,¹⁷⁹ which states that "[s]ubsection (a) of § 506 provides that a claim is secured only to the extent of the value of the property on which the lien is fixed; the remainder of that claim is considered unsecured."¹⁸⁰ Relying on the *Ron Pair* definition, courts adopting the majority view hold that § 506 determines the extent to which a claim is secured and, therefore, § 1322(b)(2) does not bar bifurcation of a mortgagee's claim into unsecured and secured portions.¹⁸¹

Third, the courts adopting the majority view note that their construction of §§ 1322(b)(2) and 506(a) allow the two sections to be read in harmony.¹⁸² As the *Demoff* court contends:

[T]he assertion that § 506(a) and § 1322(b)(2) conflict, and that because of this conflict the specific language of § 1322(b)(2) must prevail over the general language of § 506(a), [is incorrect]. These two sections do not conflict and when read in the context of the entire Bankruptcy Code they are harmonious and internally consistent.¹⁸³

Fourth, they argue that their interpretation does not render § 1322(b)(2) meaningless.¹⁸⁴ As the Third Circuit states:

[S]ection 1322(b)(2) continues [under this interpretation] to prevent modification of the rights of holders of a secured claim secured only by a real estate interest in the debtor's

176. *Simmons*, 78 B.R. at 303-04 (emphasis added).

177. *Id.*

178. *Hart*, 923 F.2d at 1415 n.4; *Houghland*, 886 F.2d at 1183; *Secor Bank*, 129 B.R. at 465; *Gadson*, 114 B.R. at 456; *Brouse*, 110 B.R. at 543; *Harris*, 94 B.R. at 836; *Kehm*, 90 B.R. at 120.

179. 489 U.S. 235 (1989).

180. *Id.* at 239.

181. *Houghland*, 886 F.2d at 1183; *Secor Bank*, 129 B.R. at 465.

182. *Wilson*, 895 F.2d at 128; *Brouse*, 110 B.R. at 543; *Demoff*, 109 B.R. at 920; *Frost*, 96 B.R. at 807; *Caster*, 77 B.R. at 13.

183. *Demoff*, 109 B.R. at 920.

184. *Wilson*, 895 F.2d at 128; *Brouse*, 110 B.R. at 543; *Frost*, 96 B.R. at 807.

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home, rights that in the absence of the exclusionary language could be modified under Chapter 13.¹⁸⁵

Fifth, courts adopting the majority view argue that bifurcation will have a minimal impact on lenders.¹⁸⁶ As to “undersecured mortgage holders, they will be receiving what they would receive if the real estate were foreclosed on . . . outside the framework of bankruptcy, and will suffer no undue prejudice by the application of § 506(a).”¹⁸⁷ Under foreclosure, the lenders would receive no more than fair market value, the same as what they would receive under bifurcation.¹⁸⁸

Finally, courts adopting the majority view assert that their interpretation fulfills both the “fresh start” purpose of bankruptcy¹⁸⁹ and the congressional purpose behind § 1322(b)(2).¹⁹⁰ Courts adopting the majority view reason that it would be inconsistent with the fresh start purposes of the Bankruptcy Code for a creditor “to do better under [a] [d]ebtor’s Chapter 13 plan than if [the] debtors had not filed at all.”¹⁹¹ Similarly, a more “convincing interpretation of [the] congressional intent in enacting § 1322(b)(2) . . . is posited in the context of the Congressional intention ‘to make available the [C]hapter 13 remedy to a wide range of financially distressed debtors, including those debtors who may have one or more mortgages on their homes.’ ”¹⁹² Consequently, “[t]he statutory scheme of Chapter 13 must be fairly read to permit those debtors to effectively deal with mortgage creditors” by allowing them to utilize § 506(a) in their Chapter 13 plan.¹⁹³

D. *The Northern District of Georgia’s View*

In *Wright v. C&S Family Credit, Inc.*,¹⁹⁴ the issue of the extent of § 1322(b)(2)’s protection of residential mortgagees was

185. *Wilson*, 895 F.2d at 128.

186. *Gadson*, 114 B.R. at 456; *Demoff*, 109 B.R. at 921; *Caster*, 77 B.R. at 13.

187. *Demoff*, 109 B.R. at 921.

188. *Id.*

189. *Harris*, 94 B.R. at 836-37; *Simmons*, 78 B.R. at 304.

190. *Caster*, 77 B.R. at 13.

191. *Harris*, 94 B.R. at 837 (citing *In re Houghland*, 93 B.R. 718, 723 (D. Or. 1988), *aff’d*, 886 F.2d 1182 (9th Cir. 1989)).

192. *Caster*, 77 B.R. at 13 (citing *In re Neal*, 10 B.R. 535, 539 (Bankr. S.D. Ohio 1981)).

193. *Neal*, 10 B.R. at 540.

194. 128 B.R. 838 (Bankr. N.D. Ga. 1991).

considered in Georgia for the first time. *Wright* involved an attempt by an Atlanta woman to bifurcate the undersecured first mortgage on her home into secured and unsecured claims pursuant to § 506(a)¹⁹⁵ of the Bankruptcy Code. The mortgagee, C&S Family Credit, however, objected to her Chapter 13 plan, arguing that it modified the terms of a security interest in real property that was the debtor's principal residence and was thus in violation of § 1322(b)(2).¹⁹⁶

Two issues were considered in *Wright*. First, whether a security deed which took an interest in "all machinery, apparatus, equipment, fittings and fixtures, whether actually or constructively attached to said property," in "all rights, title and interest of Grantor in and to the minerals, flowers, shrubs, crops, trees, timber and other emblements," in "returned, unearned and payable insurance premiums," and in "rents and profits" after a default constituted additional collateral which placed the lender outside of § 1322(b)(2)'s protection for holders of claims secured *only* by the debtor's principal residence.¹⁹⁷ The second issue was whether a Chapter 13 petition could bifurcate an undersecured mortgage into secured and unsecured portions pursuant to § 506(a) without violating the antimodification clause of § 1322(b)(2).¹⁹⁸

As to the issue of additional collateral, the *Wright* court found that none of the above-cited items constituted a security interest in something other than the debtor's principal residence.¹⁹⁹ The court first held that a bare security interest in fixtures and other items "actually or constructively attached" to the residence did not remove the loan from § 1322(b)(2) protection.²⁰⁰ The court reasoned that personal property which is actually or constructively attached to real property is considered part of the realty under Georgia law.²⁰¹ Code section 11-9-313(3)²⁰² allows the "creation of an encumbrance upon fixtures pursuant to

195. *Id.*

196. *Id.*

197. *Id.* at 841

198. *Id.*

199. *Id.* at 842.

200. *Id.* at 843-44.

201. *Id.*

202. O.C.G.A. § 11-9-313(3) (1982). The statute states: "This article does not prevent the creation of an encumbrance upon fixtures pursuant to real estate law." *Id.* O.C.G.A. § 11-9-313 deals with the priority of security interests in fixtures.

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real estate law."²⁰³ In fact, section 11-9-313(1)(a)²⁰⁴ defines "fixtures" as "goods" which "become so related to particular real estate that an interest in them arises under real estate law."²⁰⁵ The presumption that fixtures are part of the realty is an old and established doctrine in Georgia. In 1937, in *Consolidated Warehouse Co. v. Smith*,²⁰⁶ realty was defined to include "all lands and the buildings thereon, and all things permanently attached to either, or any interest therein or issuing out of or dependent thereon."²⁰⁷ The presumption that fixtures are part of the realty can, however, be defeated.²⁰⁸ Code section 11-9-313²⁰⁹ allows for the creation of a security interest in fixtures

203. *Id.*

204. O.C.G.A. § 11-9-313(1)(a) (1982). The statute reads: "Goods are 'fixtures' when they become so related to particular real estate that an interest in them arises under real estate law." *Id.*

205. *Id.*

206. 189 S.E. 724 (Ga. Ct. App. 1937).

207. *Id.*

208. *See* O.C.G.A. § 11-9-313 (1982).

209. *Id.* The statute reads in relevant part:

(2) A security interest under this article may be created in goods which are fixtures or may continue in goods which become fixtures

. . . .

(4) A perfected security interest in fixtures has priority over the conflicting interest of an encumbrancer or owner of the real estate where:

(a) The security interest is a purchase money security interest, the interest of the encumbrancer or owner arises before the goods become fixtures, the security interest is perfected by a fixture filing before the goods become fixtures or within ten days thereafter, and the debtor has an interest of record in the real estate or is in possession of the real estate; or

(b) The security interest is perfected by a fixture filing before the interest of the encumbrancer or owner is of record, the security interest has priority over any conflicting interest of a predecessor in title of the encumbrancer or owner, and the debtor has an interest of record in the real estate or is in possession of the real estate; or

(c) The fixtures are readily removable factory or office machines or readily removable replacements of domestic appliances which are consumer goods, and before the goods become fixtures the security interest is perfected by any method permitted by this article; or

(d) The conflicting interest is a lien on the real estate obtained by legal or equitable proceedings after the security interest was perfected by any method permitted by this article; or

(e) The security interest is a purchase money security interest in readily removable carpeting or padding for carpeting, the interest of the encumbrancer or owner arises before the goods become fixtures, and the security interest is perfected by fixture

as personalty and not as realty.²¹⁰ The court in *Wright* held that the security deed at issue did not specifically establish an interest in fixtures as personalty and did not reach beyond recognizable interests in fixtures as realty.²¹¹

As to the security interest in rents and profits, the court ruled that they were "incorporeal hereditaments, which are part of the possessory bundle of rights known as seizin and are, therefore, inextricably bound to the real property itself."²¹² In *Stevens v. Worrill*,²¹³ the Georgia Supreme Court ruled that one in possession of land is entitled to the rents and profits growing out of that land until the institution of an appropriate action to recover the land is taken by the holder of a security interest in the land.²¹⁴ Since C&S was entitled to the rents and profits only after a default had occurred and C&S had taken actual or constructive possession of the property,²¹⁵ the rights of C&S to rents and profits did not constitute separate items of collateral.²¹⁶

filing before the goods become fixtures.

(5) A security interest in fixtures, whether or not perfected, has priority over the conflicting interest of an encumbrancer or owner of the real estate where:

(a) The encumbrancer or owner has consented in writing to the security interest or has disclaimed an interest in the goods as fixtures; or

(b) The debtor has a right to remove the goods as against the encumbrancer or owner. If the debtor's right terminates, the priority of the security interest continues for a reasonable time.

Id.

210. *Id.*

211. *Wright*, 128 B.R. at 843.

212. *Id.*

213. 73 S.E. 366 (Ga. 1911).

214. *Id.*

215. *Wright*, 128 B.R. at 841.

216. *Id.* at 844. Three months after *Wright*, a Bankruptcy Court for the Southern District of Georgia also considered the issue of whether a mortgagee's security interest in escrow payments, rents, and profits in addition to the debtor's principal residence constituted additional collateral placing the creditor outside of § 1322(b)(2)'s antimodification protection. *Dent v. Associates Equity Servs. Co. (In re Dent)*, 130 B.R. 623 (Bankr. S.D. Ga. 1991). As to the rents and profits, the *Dent* court concurred with the *Wright* court's reasoning that "[t]he right to collect rents is part of the possessory bundle of rights which are inextricably bound to the real estate itself and does not constitute other security which would remove the claim . . . from the protection of § 1322(b)(2)." *Id.* at 628. The *Dent* court, however, did not find *Wright* applicable to the issue of the security interest in the escrow payments. *Id.* The *Dent* court held that escrow payments are not part of the possessory rights in real property. *Id.* at 629. Rather, the court found that "[t]he obligation to maintain

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Similarly, the court ruled that since the rights of C&S to returned, unearned, and payable insurance premiums arise only upon foreclosure, the interest in insurance premiums did not constitute additional security for the debt "in the common sense usage of the term in § 1322(b)(2)."²¹⁷ Finally, as to the security interest in the "minerals, flowers, shrubs, trees, etc." the court ruled these were clearly not additional collateral.²¹⁸ The court found the argument that a security interest in these items constituted a security interest in something other than the debtor's principal residence "unsupportable."²¹⁹

As to the bifurcation issue, the *Wright* court, adopting the majority view, held that bifurcation of an undersecured claim secured by a debtor's residence into secured and unsecured portions pursuant to § 506(a) does not modify that claim in violation of § 1322(b)(2).²²⁰ The court first noted that the

property insurance is a covenant contained in the deed to secure debt and is a contractual obligation between the debtor and the lender. The cash escrow payments are separate and distinct from the real property." *Id.* Consequently, Associates' present security interest in the escrow payments constituted additional collateral, and its claim, therefore, was secured by more than an interest in real property which is the debtor's principal residence. *Id.* The *Dent* court rejected Associates' argument that it held an unperfected security interest in the escrow payments. *Id.* The court noted that the debtor made payments directly to Associates for deposit in the escrow account and, consequently, that Associates, under Georgia law, perfected its security interest by possession. *Id.* (citing O.C.G.A. § 11-9-305 (1982), which provides in pertinent part: "A security interest in letters of credit and advises of credit . . . , goods, instruments, money, negotiable documents, or chattel paper may be perfected by the secured party's taking possession of the collateral"). The *Dent* court also rejected Associates' contention that it had released the escrow payments to the debtor and, therefore, retained the protection of § 1322(b)(2). *Dent*, 130 B.R. at 629. The court recognized that, under Georgia law, a secured creditor may release all or part of its collateral securing its claim against the debtor but ruled that a secured creditor cannot, postpetition, improve its position against the bankruptcy petitioner by releasing its lien against only part of its collateral. *Id.* distinguishing O.C.G.A. § 11-9-406 (Supp. 1992), which provides in pertinent part: "A secured party of record may by his signed statement release all or a part of any collateral described in a filed financing statement." *Id.* Rather, Associates' postpetition release is "irrelevant" for purposes of § 1322(b)(2) analysis, and, since it held a perfected security interest at the time of the debtor's filing under Chapter 13, the interest in escrow payments constitutes additional collateral. *Dent*, 130 B.R. at 630 (citing *In re Baksa*, 5 B.R. 184, 187 (Bankr. N.D. Ohio 1980)).

217. *Wright*, 128 B.R. at 844. The court also noted that the rights of C&S to returned, unearned, and payable insurance premiums were not included in the description of the collateral in the habendum clause of the security deed. *Id.*

218. *Id.*

219. *Id.*

220. *Id.* at 847.

legislative history offered no conclusive or definitive resolution to the issue.²²¹ Consequently, the court looked to the language of the two statutes and at precedent to determine the issue.²²² The court recognized that the only precedent in the Eleventh Circuit was *In re Chavez*²²³ but found its reasoning unpersuasive; therefore, the court declined to follow it.²²⁴

In its analysis, the court argued that § 1322(b)(2) does not expressly exclude application of § 506(a).²²⁵ Moreover, it asserted that bifurcation pursuant to § 506(a) does not negate application of the antimodification clause of § 1322(b)(2).²²⁶ Rather, § 1322(b)(2) prevents modification to the extent that the mortgagee's claim is secured.²²⁷ The court explained:

[A]pplication of § 506 to bifurcate a claim secured by a debtor's residence does not negate application of the anti-modification provisions of § 1322(b)(2). Bifurcation results in modification of the principal amount of the secured claim. Other rights of the holder of the secured claim remain and are protected by § 1322(b)(2).²²⁸

The court, however, recognized that its analysis led to some significant postbifurcation issues.²²⁹ Due to the reduced amount of the secured debt after bifurcation, some modification of the terms of the mortgage was required.²³⁰ Without deciding, the court recognized two possible solutions.²³¹ First, the maturity date of the mortgage agreement could be modified while leaving the monthly payments the same.²³² Second, the term could remain the same and monthly payments would be lowered according to the reduction in the principal.²³³ In either case, the

221. *Id.* at 845.

222. *Id.* at 844-47.

223. 117 B.R. 733 (Bankr. S.D. Fla. 1990). The *Chavez* court held that § 1322(b)(5) contained the only permissible modification of a claim secured only by a debtor's principal residence; consequently, bifurcation pursuant to § 506(a) was impermissible. *Id.*

224. *Wright*, 128 B.R. at 847.

225. *Id.*

226. *Id.*

227. *Id.*

228. *Id.*

229. *Id.* at 847-48.

230. *Id.* at 848.

231. *Id.*

232. *Id.*

233. *Id.*

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court recognized that § 1322(b)(2) prevented a change in the interest rate on the mortgage.²³⁴

IV. CHAPTER 13 CRAMDOWN AFTER *DEWSNUP V. TIMM*

Although it involved a Chapter 7 case, the decision of the United States Supreme Court in *Dewsnup v. Timm*²³⁵ has redefined the debate in Chapter 13 cramdown cases.²³⁶ The Supreme Court held that a Chapter 7 debtor may not apply § 506(a)²³⁷ and (d)²³⁸ to strip down a mortgage lien.²³⁹ Creditors have argued by analogy that a Chapter 13 debtor may not strip down her mortgage lien, and courts have split on whether *Dewsnup* has such an implication for Chapter 13 cases.²⁴⁰

A. *Dewsnup v. Timm*1. *History of the Case*

In June of 1978, debtors Aletha and T. LaMar Dewsnup granted a lien on two parcels of farmland they owned as collateral for a loan of \$119,000.²⁴¹ The Dewsnups defaulted the next year, and their creditors proceeded, pursuant to the terms of the debt, to foreclose on the Dewsnups' farmland.²⁴² Before the foreclosure sale, Aletha Dewsnup, after two prior chapter 11

234. *Id.*

235. 112 S. Ct. 773 (1992). For a discussion of *Dewsnup*'s import for Chapter 7 cases, see Alan P. Woodruff, *Lien Stripping in Chapter 7 Bankruptcy After Dewsnup v. Timm*, 66 FLA. B.J. 31 (1992).

236. See, e.g., *Lomas Mortgage v. Wiese*, 980 F.2d 1279 (9th Cir. 1992); *Nobleman v. American Sav. Bank (In re Nobleman)*, 968 F.2d 483 (5th Cir. 1992); *Sapos v. Provident Inst. of Sav.*, 967 F.2d 918 (3d Cir. 1992); *Bellamy v. Federal Home Loan Mortgage Corp. (In re Bellamy)*, 962 F.2d 176 (2d Cir. 1992).

237. 11 U.S.C. § 506(a) (1988). For the text of the statute, see *supra* note 23.

238. 11 U.S.C. § 506(d) (1988). The statute reads in pertinent part: "To the extent that a lien secures a claim against the debtor that is not an allowed secured claim, such lien is void." *Id.*

239. *Dewsnup*, 112 S. Ct. at 778.

240. Compare *Lomas Mortgage v. Wiese*, 980 F.2d 1279 (9th Cir. 1992) and *Sapos v. Provident Inst. of Sav.*, 967 F.2d 918 (3d Cir. 1992) and *Bellamy v. Federal Home Loan Mortgage Corp. (In re Bellamy)*, 962 F.2d 176 (2d Cir. 1992) with *Nobleman v. American Sav. Bank (In re Nobleman)*, 968 F.2d 483 (5th Cir. 1992).

241. *Dewsnup*, 112 S. Ct. at 775.

242. *Id.*

petitions were dismissed, filed a petition seeking liquidation under Chapter 7 of the Bankruptcy Code.²⁴³

In 1987, debtor Dewsnap, as part of her Chapter 7 case, filed an adversary proceeding seeking pursuant to § 506 to avoid a portion of her creditors' lien.²⁴⁴ Dewsnap argued that § 506(a)²⁴⁵ allows her to void the creditors' lien to the extent that it exceeds the fair market value of the farmland²⁴⁶ and that § 506(d)²⁴⁷ then allows her to redeem the property by tendering the assessed market value to the creditors in cash.²⁴⁸ The bankruptcy court refused to grant this relief, reasoning that once the property was abandoned by the trustee, it no longer fell within the reach of § 506(a),²⁴⁹ which applies only to "property in which the estate has an interest."²⁵⁰

After the district court summarily affirmed the bankruptcy court's decision, the Tenth Circuit Court of Appeals also affirmed.²⁵¹ The Tenth Circuit found that a claim is subject to reduction in security pursuant to § 506(a) only when the estate has an interest in the property, and since the estate had no interest in the abandoned property, the debtor could not utilize § 506(a) and (d) to reduce the value of the lien and then redeem the property.²⁵² The Tenth Circuit further reasoned that a contrary result would be inconsistent with § 722,²⁵³ under

243. *Id.* at 776.

244. *Id.*

245. 11 U.S.C. § 506(a) (1988). For the text of the statute, see *supra* note 23.

246. At the time of the trial, the bankruptcy court valued the land at \$39,000. *Dewsnap*, 112 S. Ct. at 776.

247. 11 U.S.C. § 506(d) (1988). The statute reads in pertinent part: "To the extent that a lien secures a claim against the debtor that is not an allowed secured claim, such lien is void." *Id.*

248. *Dewsnap*, 112 S. Ct. at 776; *Dewsnap v. Timm* (*In re Dewsnap*), 908 F.2d 588, 589 (10th Cir. 1990), *aff'd*, 112 S. Ct. 773 (1992). The bankruptcy trustee had abandoned the property pursuant to 11 U.S.C. § 554(a). *Dewsnap v. Timm* (*In re Dewsnap*), 908 F.2d 588, 589 (10th Cir. 1990), *aff'd*, 112 S. Ct. 773 (1992).

249. 11 U.S.C. § 506(a) (1988). For the text of the statute, see *supra* note 23.

250. *Dewsnap*, 112 S. Ct. at 776 (citing *In re Dewsnap*, 87 B.R. 676 (Bankr. D. Utah 1988), *aff'd*, 908 F.2d 588 (10th Cir. 1990), *aff'd*, 112 S. Ct. 773 (1992)).

251. *Dewsnap*, 112 S. Ct. at 776 (citing *Dewsnap v. Timm* (*In re Dewsnap*), 908 F.2d 588 (10th Cir. 1990), *aff'd*, 112 S. Ct. 773 (1992)).

252. *Dewsnap*, 112 S. Ct. at 776 (citing *Dewsnap v. Timm* (*In re Dewsnap*), 908 F.2d 588, 590-91 (10th Cir. 1990), *aff'd*, 112 S. Ct. 773 (1992)).

253. 11 U.S.C. § 722 (1988). The statute states, in relevant part:

An individual debtor may . . . redeem tangible personal property . . . from a lien securing a dischargeable consumer debt, if such property . . . has been abandoned under section 554 of this title, by paying the holder of such lien the amount of the allowed secured claim of such holder that

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which a debtor has a limited right to redeem certain personal property.²⁵⁴

2. *The Decision of the United States Supreme Court*

The Supreme Court of the United States affirmed, holding that § 506(d) does not allow a debtor to strip down a lien to the fair market value of the collateral when the creditor's claim is secured by a lien that has been fully allowed pursuant to § 502.²⁵⁵ The Court ruled that the creditors' claim therefore could not be classified as "not an allowed secured claim" for the purposes of the lien-voiding provision of § 506(d),²⁵⁶ and consequently, that the debtor could not utilize § 506(d) to redeem the property.²⁵⁷

In making this determination, the Court rejected Dewsnup's argument that, since § 506(a) establishes the allowed amount of a "secured claim" and § 506(d) voids a lien to the extent that the lien is not an "allowed secured claim," the undersecured portion of the creditors' lien was void.²⁵⁸ Although the Court recognized that § 506(a) and (d) referred to an "allowed secured claim," it ruled that the meaning of "allowed secured claim" in § 506(d) need not be defined by reference to § 506(a) and, in fact, that the phrase "allowed secured claim" did not have the same meaning in § 506(d) as in § 506(a).²⁵⁹

The court argued that the phrase "allowed secured claim" did not have the same meaning in § 506(d) as in 506(a) because the legislative history was completely devoid of any mention of a Congressional intent to change the pre-Code rule that liens on real property pass through bankruptcy unaffected.²⁶⁰ The Court stated:

is secured by such lien.

Id.

254. *Dewsnup*, 112 S. Ct. at 776 (citing *Dewsnup v. Timm (In re Dewsnup)*, 908 F.2d 588, 592 (10th Cir. 1990), *aff'd*, 112 S. Ct. 773 (1992)).

255. *Dewsnup*, 112 S. Ct. at 778-79 (citing 11 U.S.C. § 502 (1988)). The statute reads, in relevant part: "A claim or interest . . . is deemed allowed, unless a party in interest . . . objects." *Id.*

256. 11 U.S.C. § 506(d) (1988). For the text of the statute, see *supra* note 238.

257. *Dewsnup*, 112 S. Ct. at 778-79.

258. *Id.* at 776-78.

259. *Id.*

260. *Id.* at 779.

[G]iven the ambiguity here, to attribute to Congress the intention to grant a debtor the broad new remedy against allowed claims to the extent that they become "unsecured" for purposes of § 506(a) without the new remedy's being mentioned somewhere in the Code itself or in the annals of Congress is not plausible, in our view, and is contrary to basic bankruptcy principles.²⁶¹

The Court reasoned further that a lien passes through bankruptcy and stays with the real property until foreclosure because that is "what was bargained for" by the parties.²⁶² The Court elaborated, stating that:

The voidness language sensibly applies only to the security aspect of the lien and then only to the real deficiency in the security. Any increase over the judicially determined valuation during bankruptcy rightly accrues to the benefit of the creditor, not to the benefit of the debtor and not to the benefit of other unsecured creditors whose claims have been allowed and who had nothing to do with the mortgagor-mortgagee bargain.²⁶³

B. Interpretations of § 1322(b)(2) After Dewsnap

The first appeals court to consider the issue of Chapter 13 mortgage cramdown after the Supreme Court's decision in *Dewsnap* was the Second Circuit. In *Bellamy v. Federal Home Loan Mortgage Corp.*,²⁶⁴ the Second Circuit found that *Dewsnap* was not applicable to Chapter 13 cases and therefore held that the bifurcation of the residential mortgagee's claim was not an improper modification of rights under § 1322(b)(2).²⁶⁵

In *Bellamy*, the creditor, Federal Home, noted that courts that allow bifurcation contend that the determination of the extent of

261. *Id.*

262. *Id.* at 778.

263. *Id.*

264. 962 F.2d 176 (2d Cir. 1992).

265. *Id.* Other cases in which bifurcation has been found admissible in Chapter 13 after *Dewsnap* include: *Lomas Mortgage v. Wiese*, 980 F.2d 1279 (9th Cir. 1992); *Sapos v. Provident Inst. of Sav.*, 967 F.2d 918 (3d Cir. 1992); *Union Mortgage Co. v. Avret (In re Avret)*, 146 B.R. 47 (Bankr. S.D. Ga. 1992); *Union Planters Nat'l Bank v. Sainz-Dean (In re Sainz-Dean)*, 143 B.R. 784 (D. Colo. 1992); *In re Dyer*, 142 B.R. 364 (Bankr. D. Ariz. 1992); *In re Cardinale*, 142 B.R. 42 (Bankr. D.R.I. 1992); *In re Mann*, 1992 WL 355430 (Bankr. M.D. Ga. Nov. 23, 1992); *Taras v. Commonwealth Mortgage Corp. (In re Taras)*, 136 B.R. 941 (Bankr. E.D. Pa. 1992).

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a “secured claim” pursuant to § 1322(b)(2) must be made by reference to § 506(a).²⁶⁶ Federal Home, however, argued that since *Dewsnup* found that “secured claim” in § 506(d) does not have the same meaning as it does in § 506(a), the term does not have the same meaning in § 1322(b)(2) as it does in § 506(a).²⁶⁷ Federal Home further argued that § 1322(b)(2), when read internally and without reference to § 506(a), clearly protects a mortgagee’s rights and prohibits the modification of those rights by techniques such as bifurcation, which reduces the ultimate value of the creditor’s right to payment under the mortgage contract.²⁶⁸

The Second Circuit, however, rejected Federal Home’s analysis. In rejecting Federal Home’s arguments, the Second Circuit noted that “*Dewsnup* did not hold that ‘secured claim’ in other provisions of the Code was never to be construed as it was in § 506(a).”²⁶⁹ Rather, the court found that the issue of “whether ‘secured claim’ has the same meaning as it does in § 506(a) must be determined with reference to the particular Code provision at issue.”²⁷⁰ The Second Circuit made such an analysis and ultimately determined that “secured claim” has the same meaning in § 1322(b)(2) as it does in § 506(a).²⁷¹

In making this determination, the court began with the presumption that “‘secured claim’ ordinarily has the meaning assigned to it in § 506(a)” because certain Code provisions explicitly state that the term “secured claim” is not to be defined as in § 506(a).²⁷² This presumption, moreover, will only be overcome in those rare cases, like *Dewsnup*, where construing “secured claim” with the meaning assigned to it in § 506(a) would be “contrary to basic bankruptcy principles.”²⁷³ The Second Circuit found no such circumstances with regard to § 1322(b)(2).²⁷⁴ As the court said:

[D]istinct from its treatment of liens [in section 506(d)], the Code *expressly* contemplates that a Chapter 13 debtor’s plan

266. *Bellamy*, 962 F.2d at 182.

267. *Id.*

268. *Id.* at 179.

269. *Id.* at 182.

270. *Id.*

271. *Id.* at 183-84.

272. *Id.* at 182 (citing 11 U.S.C. § 1111(b)(2) (1988)).

273. *Id.* (quoting *Dewsnup*, 112 S. Ct. at 779).

274. *Id.* at 183-84.

of reorganization may today, contrary to pre-Code practice, deal with creditors whose claims are secured by real property As a result, applying § 1322(b)(2) in light of § 506(a) does not alter well-settled bankruptcy principles. To the contrary, it furthers Congress' scheme under Chapter 13 by allowing the adjustment of claims secured by real property.²⁷⁵

The court therefore concluded that "allowing Chapter 13 debtors to strip down an undersecured residential mortgagee's claim forwards the legislative purpose of furthering reorganizations for individuals with regular income to enable them to retain their homes."²⁷⁶

Two other circuit courts also found *Dewsnup* unpersuasive in Chapter 13 cramdown cases.²⁷⁷ Although both the Ninth and Third Circuits considered *Dewsnup* compelling enough to warrant reconsideration of their earlier decisions allowing Chapter 13 mortgage cramdowns, they ultimately reaffirmed those earlier decisions.²⁷⁸ In doing so, both courts relied on the Second Circuit's analysis in *Bellamy*.²⁷⁹

The Fifth Circuit, on the other hand, did not find *Bellamy* persuasive when it considered the issue of Chapter 13 mortgage cramdown and thereby became the first circuit court to rule that Chapter 13 debtors could not bifurcate mortgage lien claims on their principal residence into secured and unsecured claims.²⁸⁰ In contrast to the other Circuits, the Fifth Circuit found that the "Supreme Court's recent decision in *Dewsnup v. Timm* . . . lends support to [the] view that bifurcation is impermissible."²⁸¹

275. *Id.*

276. *Id.* at 184.

277. *Lomas Mortgage v. Wiese*, 980 F.2d 1279 (9th Cir. 1992); *Sapos v. Provident Inst. of Sav.*, 967 F.2d 918 (3d Cir. 1992).

278. *Lomas Mortgage v. Wiese*, 980 F.2d 1279 (9th Cir. 1992), *aff'g* *Houghland v. Lomas & Nettleton Co. (In re Houghland)*, 886 F.2d 1182 (9th Cir. 1989); *Sapos v. Provident Inst. of Sav.*, 967 F.2d 918 (3d Cir. 1992), *aff'g* *Wilson v. Commonwealth Mortgage Corp.*, 895 F.2d 123 (3d Cir. 1990).

279. *Lomas Mortgage*, 980 F.2d at 1282; *Sapos*, 967 F.2d at 924-25.

280. *Nobleman v. American Sav. Bank (In re Nobleman)*, 968 F.2d 483 (5th Cir. 1992). Other courts that have determined that Chapter 13 mortgage cramdown was impermissible after *Dewsnup* include: *In re Barnes*, 146 B.R. 854 (Bankr. W.D. Okl. 1992); *In re Doss*, 143 B.R. 952 (Bankr. E.D. Okl. 1992); *In re Sainz-Dean*, 139 B.R. 739 (Bankr. D. Colo. 1992), *rev'd*, 143 B.R. 784 (D. Colo. 1992); *In re Ireland*, 137 B.R. 65 (Bankr. M.D. Fla. 1992); *In re Strober*, 136 B.R. 614 (Bankr. E.D.N.Y. 1992); *In re Davidoff*, 136 B.R. 567 (Bankr. M.D. Fla. 1992).

281. *Nobleman*, 968 F.2d at 487.

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Besides the *Dewsnup* decision, the Fifth Circuit considered two other factors in making its determination. First, the court considered the “plain meaning” of § 1322(b)(2) and found that it “clearly prohibits the modification of rights of holders of secured claims if the claim is secured only by a security interest in the debtor’s principal residence.”²⁸² Although the court recognized that the “prohibition in section 1322(b)(2) appears to conflict with section 506(a),” the court applied the tenet of statutory construction that the specific prevails over the general and therefore held that “the specific language of section 1322(b)(2) prevails over the general language of section 506(a).”²⁸³

The court also distinguished § 1322(b)(2) from § 506(a) by noting the former’s emphasis on “the rights of holders of” claims as opposed to the latter’s emphasis on the modification of “claims.”²⁸⁴ As the court explained:

[S]ection 1322(b)(2) describes its subject matter as the modification of “the *rights of holders of*” claims, not as the modification of *claims* as such; thus, the section can properly be read as *excepting* from its reach modification of “*the rights of holders of . . . a claim secured only by a security interest in real property that is the debtor’s principal residence . . .*” Therefore, even if the entirety of such claim is not a secured claim (as per section 506(a)), the rights of a holder of such a claim may not be modified under section 1322(b)(2).²⁸⁵

Second, the Fifth Circuit found that the legislative history of § 1322(b)(2) barred modification.²⁸⁶ The court said:

With regard to § 1322(b)(2), the Senate receded from its position that no “modification” was to be permitted of *any* mortgage secured by real estate; it instead agreed to a provision that modification was to be barred *only* as to a claim “secured only by a security interest in real property *that is the debtor’s principal residence*.” This limited bar was apparently in response to perception, or to suggestions advanced in the legislative hearings . . . that, home-mortgage

282. *Id.* at 487-88.

283. *Id.* at 488.

284. *Id.*

285. *Id.*

286. *Id.*

lenders, performing a valuable social service through their loans, needed special protection against modification.²⁸⁷

The Fifth Circuit, therefore, found this desire to protect the home mortgage industry controlling.²⁸⁸

Consequently, the Supreme Court's decision in *Dewsnup v. Timm* has changed the nature of the debate about Chapter 13 mortgage cramdown but not the result.²⁸⁹ The courts continue to remain deeply divided on the permissibility of a debtor's attempt to bifurcate an undersecured home mortgage with the ultimate end of reducing the value of the mortgage to the current value of the debtor's home.

V. THE FAILURE OF THE 102D CONGRESS TO STATUTORILY RESOLVE THE DEBATE

As both mortgagors and mortgagees in many communities face lower property and home values,²⁹⁰ the debate over both the validity and the impact of residential mortgage cramdown grows.²⁹¹ Debtors and their advocates argue that bifurcation should be allowed because it furthers the bankruptcy principle of a fresh start.²⁹² They argue that this is especially true for a debtor's home because this is usually the only significant asset the debtor has in a Chapter 13 case.²⁹³ Moreover, debtors' advocates contend that lenders receive no less after the mortgage cramdown than they would receive under foreclosure—the market value of the home.²⁹⁴

287. *Id.* at 488-89.

288. *Id.* at 489.

289. *Compare* *Lomas Mortgage v. Wiese*, 980 F.2d 1279 (9th Cir. 1992) and *Sapos v. Provident Inst. of Sav.*, 967 F.2d 918 (3d Cir. 1992) and *Bellamy v. Federal Home Loan Mortgage Corp.* (*In re Bellamy*), 962 F.2d 176 (2d Cir. 1992) with *Nobleman v. American Sav. Bank* (*In re Nobleman*), 968 F.2d 483 (5th Cir. 1992).

290. Charles Haddad, *Depreciation: Sellers Suffer as Home Values Plunge, Competition Rises*, ATLANTA CONST., Nov. 11, 1991, at D1.

291. Haddad, *supra* note 290, at D1; Canzoneri, *supra* note 18, at 17; Cataldo, *supra* note 64; Tracy J. Cowan, Comment, *Modification of an Undersecured Home Mortgage in a Chapter 13 Proceeding*: *Houghland v. Lomas & Nettleton Co.* (*In re Houghland*), 56 MO. L. REV. 841 (1991); Regina L. Nassen, *Bankruptcy Code § 1322(b)(2)'s No-Modification Clause: Who Does It Protect?*, 33 ARIZ. L. REV. 979 (1991).

292. *In re Harris*, 94 B.R. 832, 836-37 (D.N.J. 1989); *In re Simmons*, 78 B.R. 300, 304 (Bankr. D. Kan. 1987).

293. Cataldo, *supra* note 64, at 234. Cataldo states Chapter 13 debtors "only chance at financial rehabilitation require[s] changes in the obligations secured by the debtor's residence." *Id.*

294. See 11 U.S.C. § 1325(a)(4); *In re Demoff*, 109 B.R. 902, 921 (Bankr. N.D. Ind.

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Lenders, on the other hand, contend that the analysis of the debtor is flawed. Chapter 13 residential mortgage cramdowns often require lenders to write off tens of thousands of dollars per loan.²⁹⁵ Such losses could have a profound impact on an already troubled banking industry.²⁹⁶ Such losses may also negatively impact homebuyers, who might find it more difficult to buy houses as lenders tighten restrictions on loans in response to the losses suffered due to cramdowns.²⁹⁷ Some commentators even suggest that redlining might occur if residential mortgage cramdown becomes too prevalent.²⁹⁸

Lenders also contend that residential mortgage cramdown was exactly what Congress intended to prevent when it adopted the no-modification clause in § 1322(b)(2).²⁹⁹ Since, however, this intent is obviously not clear, legislation was introduced by Senator Heflin last year to clarify the extent of the protection given by § 1322(b)(2).³⁰⁰ Although this bill ultimately did not pass, it and the changes it underwent in the most recent session of Congress show the extent of the debate over residential mortgage cramdown and indicate where the debate is headed.

As originally introduced, Senate Bill 1985 would have inserted the following provision in § 1322(b)(2):

but the plan may not modify a claim pursuant to section 506 of a person holding a primary security interest in real property or a manufactured home . . . that is the debtor's principal residence.³⁰¹

Obviously, this change reflects a Congressional concern with protecting long-term, purchase-money mortgagees.³⁰² Senator Heflin, in a speech on the Senate floor, stated that this "most important" provision:

1989).

295. Canzoneri, *supra* note 18, at 20.

296. Nassen, *supra* note 291, at 1006.

297. *In re Demoff*, 109 B.R. 902, 921 (Bankr. N.D. Ind. 1989); Nassen, *supra* note 291, at 1006.

298. Polk, *supra* note 11, at 294-98. In his article, Polk gives a detailed discussion of why redlining would occur in the mortgage industry. *Id.*

299. *Id.* at 281; Cataldo, *supra* note 64, at 227; Nassen, *supra* note 291, at 1006.

300. S. 1985, 102d Cong., 1st Sess. (1991).

301. *Id.* § 310.

302. In fact, many commentators believe that such protection was the intent of Congress in the original (and present) Code section. See Nassen, *supra* note 291, at 998-1002.

would protect the mortgage-backed securities market, and address the issue of cramdowns in chapter 13 bankruptcies This section would completely protect the entire claim in cases of first mortgages on residential real estate The section would generally protect junior security interests except in circumstances where the security interest was undersecured at the time of contracting, and only could be subject to a cramdown to the extent it remains undersecured at the time of the bankruptcy.³⁰³

Senator Heflin recognized that his proposed amendment of § 1322(b)(2) implicitly “acknowledge[s] a court’s ability to bifurcate residential real estate” under current law, but felt his bill would promote needed stability in the residential real estate market.³⁰⁴

After the Bill was favorably reported in the Senate, it went to the House of Representatives. There, the Bill was amended to read:

except that the rights of the holder of a claim secured by the most senior security interest in real property that is the debtor’s principal residence may not be modified to reduce the secured claim to a value that is less than the value, as of the date the security interest arose, of the creditor’s interest in the estate’s interest in such property.³⁰⁵

Senator Grassley explained that this amendment was a compromise between the House and Senate.³⁰⁶ The compromise would prevent the cramdown of first mortgages in Chapter 13, but would provide junior liens with a lesser degree of protection.³⁰⁷

On the same day as Senator Grassley’s report to the Senate on the compromise bill, Senator Heflin proposed an amendment which would have greatly extended the protection granted to lenders.³⁰⁸ Senator Heflin’s amendment not only would afford the holder of the most senior security interest special protection,

303. 138 CONG. REC. S8241, 8252 (daily ed. June 16, 1992) (statement of Sen. Heflin).

304. *Id.* at S8252-53.

305. 138 CONG. REC. S17358, 17360 (daily ed. Oct. 7, 1992) (message from the House of Representatives to the Senate).

306. *Id.* at S17363.

307. *Id.* at S17364.

308. *Id.* at S17502.

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it would have prevented the modification of "the rights of a holder of a claim secured only by a security interest in real property that is the debtor's principal residence."³⁰⁹ This amendment would have broadly expanded lender protection because it included two clauses—one that was similar to the compromise position protecting the senior lien holder and a second that protected all holders of claims secured only by a debtor's principal residence.³¹⁰

The Senate ultimately adopted the compromise bill, but the proposed "National Bankruptcy Review Commission Act" ultimately died when the House failed to pass it.

CONCLUSION

The extent of § 1322(b)(2)'s protection of mortgage lenders remains uncertain. The Supreme Court of the United States, in *Johnson v. Home State Bank*,³¹¹ upheld the use of Chapter 20 cramdown by debtors.³¹² In *Dewsnup v. Timm*,³¹³ however, the Court held that lien-stripping was improper in Chapter 7.³¹⁴ Although both decisions have had an impact on Chapter 13 litigation, the validity of Chapter 13 cramdown is still a subject of much debate and one on which the courts are divided.

The effects of cramdown, however, are not so contentious. They allow debtors to reduce the value of their mortgages over the stern and loud objections of mortgage lenders. Some members of Congress have heard the cries, but have, so far, been unsuccessful in settling the controversy.

Such failure will not put the controversy on the back burner. Rather, with the current split in the circuit courts, it is likely that the United States Supreme Court will soon hear the issue. Similarly, the banking industry will likely continue to push for a statutory clarification. Thus, it appears that this issue will continue to command the attention of the courts and Congress for some time to come.

John F. Connolly

309. *Id.*

310. *Id.*

311. 111 S. Ct. 2150 (1991).

312. *Id.*

313. 112 S. Ct. 773 (1992).

314. *Id.*

